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Agricultural and Rural Development Policies in the Baltic Countries

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Policies in the Baltic Countries

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FOREWORD

Identifying the optimum policy mix to ensure a vibrant and sustainable rural economy in the Baltic countries was the focus of the OECD's fifth meeting with the Baltic countries in the area of agro-food policies, held in Tallinn on 10-12 June 2003 and financed through the Baltic Regional Programme, of the OECD's Centre for Co-operation with Non-Members (CCNM). The Seminar continued the policy dialogue between senior policy makers in Estonia, Latvia and Lithuania and OECD member countries on structural and policy reforms in rural areas. The discussion was set in the context of high rates of unemployment and increasing poverty in many rural areas. Participants included high-level policy makers, parliamentarians, academics, and researchers from the three Baltic countries, OECD member countries, the European Commission and the FAO.

Low or volatile farm incomes and rising unemployment in some rural areas are central concerns for policy makers in many countries. With ongoing changes in the sources of farm household incomes, traditional farm policies are increasingly ineffective in addressing farm income problems. Better targeting of policies to address a diversity of rural and farm households needs is crucial. High rural unemployment is at the centre of the current debate in all three Baltic countries and there is increasing focus on developing a more comprehensive policy framework to resolving this pressing issue. Greater emphasis on specific targeting of enterprise development is a direct response to the dual concerns of low incomes and high unemployment in rural areas. A better understanding of the complex processes involved and the implications of greater diversity are crucial for policy makers so that they can respond appropriately to the changing environment. This process involves a complex set of cross sector policies including macroeconomic, labour, social, agricultural, regional and rural policies.

The reader will find the essence of the discussion about rural incomes, labour mobility and rural development, trends and challenges for the Baltics in the Executive Summary, with a more detailed summary of Workshop conclusions and implications at the end of this volume. The first set of papers provides an update on the agriculture and rural income situation in OECD countries and the Baltics, with emphasis on the similarities and differences within the context of the transition process and the domestic policy regimes. The second part of the Proceedings deals with developments in the rural labour market and the underlying factors that influence mobility across regions and countries. The third part discusses the rural and regional development strategies in the context of low incomes and high rates of unemployment. The final part of the report outlines the various policy options and policy balances needed in order to resolve these pressing issues in rural areas.

These Proceedings are produced by the OECD's Directorate for Food, Agriculture and Fisheries under the auspices of the Centre for Co-operation with Non-Members (CCNM) and published under the responsibility of the Secretary-General of the OECD.

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ACKNOWLEDGEMENTS

This publication brings together the contributions presented at the OECD Seminar on Agriculture and Rural Incomes, Labour Mobility and Rural Development Policies in Estonia, Latvia and Lithuania, held in Tallinn, Estonia on 10-12 June 2003.

The Seminar was prepared by OECD in co-operation with the Ministry of Agriculture of Estonia. Michael Ryan was responsible for design and organization of the Seminar in collaboration with Mr. Andres Oopkaup, Deputy Secretary-General for Agro-Food and Trade in the Ministry of Agriculture. Special thanks are extended to Ms. Kai Kasenurm for the Seminar logistics and to all those who provided papers and contributed to the success of the discussions. The papers were edited by Michael Ryan, with the assistance of Carina Lindberg. Thanks are also extended to Anita Lari who formatted the document and prepared it for publication, and to Brigitte de Vogüé and Stefanie Milowski for their assistance on budgetary matters.

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EXECUTIVE SUMMARY

Ongoing structural change in primary agriculture, driven by the adoption of new production technologies, has resulted in enormous changes in the rural economy in all countries. The continued fall in the terms of trade for agricultural products, and agriculture's share of GDP, has had implications for income levels, standard of living and employment in the sector. Low and volatile agricultural incomes accompanied by the need to address the outflow of surplus labour from the sector is a pressing issue facing policy makers. This development has important economic, social and political implications for sustaining a vibrant rural environment. Facilitating this long-term adjustment process and providing alternative employment opportunities, especially in rural areas, requires a careful balancing of policies including macroeconomic, labour, social, regional and sectoral policies.

Farm household income has been the centre of much debate in OECD countries and in the Baltics. Some countries have responded to perceived problems by increasing overall support to agriculture. However, many existing policies have been ineffective in raising incomes, particularly amongst those most in need, and have been very costly. In analysing incomes in agriculture it is critical to use the correct conceptual framework and income variable so as to reflect the changing nature of farm income in total household income.

For most OECD countries, the average farm household income is similar to the rest of society, but the share of farm income in total income continues to decline. However, the incidence of low income households is higher among farm households than among other households and the low-income gap is also wider for farm households. The extent to which farm households have off-farm earnings varies by country and region, and depends on several factors including, the general economic environment, structure of the household, size and type of farm, and the rate of farm support. Applying the household concept to the Baltic countries is more problematic as farming structures are more heterogeneous than in OECD countries. For example, farm types include corporate farms, family farms, subsistence and semi-subsistence farms, while the structure of farm households is also different often involving as many as three generations. In the Baltic region, farm household income fell sharply during the transition period, but in recent years income has been rising in Estonia and Latvia, due to higher output and improved labour productivity. The sources of income are also becoming more diversified with off-farm employment and social transfers representing a growing share of total income. In Lithuania, in particular, low incomes and poverty remain a serious problem in many rural areas, due to the higher dependence on agriculture, slower transformation process, the nature of land restitution and lower employment opportunities outside agriculture.

High rural unemployment, especially among young people, is a serious concern in most countries. With further economic growth and development, the outflow of surplus labour from primary industries, including agriculture, is likely to continue and may even increase. The "push and pull" forces that drive labour mobility are likely to intensify with further competition and adjustment. In many countries, there is an apparent paradox in the labour market, where shortages occur in both the demand and supply of labour. This mismatch usually reflects differences in the quality of labour, which can be resolved through specific labour market policies that focus on education and training, for

example. Overcoming constraints to labour mobility is critical, in particular, reducing constraints to human capital, administrative and legal impediments, infrastructure, as well as personal risk factors.

Rural labour markets in Estonia, Latvia and Lithuania, as well as in other transition countries, have been strongly affected by the transition process and, especially, the reorganisation of farms. The share of employment on large scale-farms in total agricultural employment has declined and employment has moved towards emerging family farms and household plots. Like in most OECD countries, there are large regional differences in the rate of unemployment across the Baltic countries. In general, the rate of unemployment tends to be lower in bigger cities, regions with a diversified industrial economy, and regions that offer good opportunities for tourism and leisure. The rise in unemployment among young people, in excess of 50% of the labour force in some rural regions, is a growing cause of concern for governments in the region. Moreover, the outflow of labour from agriculture and rural areas has raised concerns about rural depopulation and even desertification of areas where large areas of agricultural land are being abandoned.

In light of the income and unemployment problems in many rural areas, policies and strategies to promote rural development have become a high priority. In designing appropriate policies, a better understanding of the underlying economic linkages and processes that generate regional disparities is crucial. Currently, many countries implement an array of short-term measures to overcome the social spill-over effects of high rural unemployment and poverty. However, in the longer term, more sustainable solutions to these problems depend on resolving the underlying causes, which will vary across regions, and may include infrastructure constraints, poorly functioning market institutions, inadequate access to information, and lack of appropriate skills.

Traditional rural development measures in the EU have tended to focus largely on agriculture and on issues associated with income redistribution and project support. The situation in the Baltic countries, however, is quite different to that of most EU members, where the standard of living is higher and pluriactivity is more prevalent in rural areas. Moreover, the situation differs between the three Baltic countries, as reflected in the range of national rural and regional policies that are currently being implemented. The success of the LEADER programme in raising the income of households in poorer regions in many EU countries could provide a useful approach for future programmes in the Baltic countries. This programme emphasises the bottom-up approach to development and has a strong focus on developing local action groups and human capacity building through education and training. All three Baltic countries are currently implementing pre-accession programmes, notably through the SAPARD.

In summary, it is important that farm policy is not seen as synonymous with rural development policy. While they may be complementary and closely related to each other, agricultural policy is sector specific, while rural development policy is multi-sectoral. In dealing with issues of low incomes, poverty, and high rates of employment in rural areas, governments need to clearly identify and address the root causes of these problems and not the symptoms. Broad, output based measures aimed at raising incomes should be avoided as should production linked measures. Moreover, greater efforts should be made to improve on-farm performance and to enhance the overall productivity in all areas of the food chain. Policy responses are best expressed in as specific and explicit terms as possible. The key role of governments should be to enable economy-wide growth and development by focusing on macroeconomic and structural policies that would allow markets to work, building on the strengths of the countries endowments.

All the supporting documents and presentations available at the Seminar can be found at **www.oecd.org/agr/ete/** under Publications & Documents -- Proceedings -- *Agricultural and Rural Development Policies in the Baltic Countries.*

OPENING STATEMENTS

OPENING STATEMENT

Mr. Tiit Tammsaar
Minister of Agriculture
Ministry of Agriculture, Estonia

- I am glad to welcome the decision-makers and analysts here in Estonia. Every such gathering of high professionals that takes place in Estonia is an acknowledgement for us.

- I am glad that the other organizing party this time is the OECD. Because the OECD does not pay supports, as does the EC, it is rather difficult for outsiders to understand its importance. OECD is instead a very respectable analytical institution that works with different policies of its member states and therefore helps to achieve well-thought out compromises between different policy approaches.

- Co-operation with the OECD has been productive, and Estonia has learnt a lot from it. Be it measuring agricultural supports with the help of PSEs, or more broadly, the analysis of agricultural policy for which it is very difficult to find an opinion that is internationally more solid.

- We of course realise that choosing Estonia as a place for the Seminar is, on one hand, simply a question of order within the framework of the Baltic Regional Programme, but on the other hand, we still hope that the aim of this is to draw attention to the specificity of the situation in Estonia.

- Namely, Estonia has on one hand followed the recommendations of the OECD, as well as those of other international analysts of economic policy such as the WB and IMF, and applied liberal economic and agricultural policies during the past ten years.

- As a result of this shock therapy, employment in agriculture has, over the past decade, decreased from 18% to 5%, which is already very close to that of, for example, the European Union.

- Surplus labour has been drawn from agriculture to a large extent, and as a consequence, one fourth of the arable land has been left out of use and over 15% of the rural population is unemployed.

- Estonian national policies have, since the beginning, been oriented towards general rural development. But, perhaps the resources have not been sufficient and the re-motivation and teaching of people adequate, especially those who have relied completely on national arrangements.

- Dealing with such issues is naturally a problem not only for Estonia. Similar problems have been faced by the so-called old member states of the European Union, as well as other OECD countries. These problems are also present in the other candidate countries, including the Baltic States.

- Therefore, we hope to hear and learn from the OECD member states. On the other hand, we hope that this analysis will give insights to decision makers in all countries that face a significant decrease in agricultural employment.

- Therefore, I wish all the participants, first and foremost patience in listening to each other, and I hope for an active and constructive dialogue in analysing the possibilities for the future.

- Thank you for your attention and I wish you a lot of success.

OPENING STATEMENT

Mr. Ken Ash
Deputy Director, Directorate for Food, Agriculture and Fisheries
Organisation for Economic Co-operation and Development (OECD)

- Minister Tammsaar, Vice-Chancellors, State Secretaries, international organisations, ladies and gentlemen, it gives me great pleasure to welcome you, on behalf of OECD, to this joint OECD-Baltic Seminar.

- Many of you, here today, are familiar with the work of the OECD and have participated in previous Workshops and Seminars organised in the Baltic region or in Paris.

- I am glad to have the opportunity to say a few words about the long and successful co-operation between Estonia, Latvia, Lithuania and the OECD, and to briefly outline the objectives of this Seminar.

- The initial contact between the OECD Secretariat and the Baltic countries began, in 1992, with the Workshop in Visby, hosted by the Swedish Government. This Workshop set the stage for several joint activities that focused, in particular, on the transition of the agricultural sector in the Region to a more modern, market oriented, and competitive industry.

- The most intensive period of co-operation took place in 1995/96, with the preparation of the *Reviews of Agricultural Policies* in Estonia, Latvia and Lithuania. These *Reviews* provided the basis for the calculation of the PSEs/CSEs, which have been widely used in the development of policies in the Region. Several colleagues from Estonia, Latvia and Lithuania, some of whom I see here today, spent some time with the OECD in Paris contributing to this work.

- Government officials and policy experts from Estonia, Latvia and Lithuania have actively participated in the biannual meetings of the *Forum on Agricultural Policies in Non-Member countries.* Agricultural and trade policy developments in the three countries are covered in our annual *Monitoring Report* for non-member economies.

- To highlight the importance of co-operation between OECD and the three Baltic countries, a special regional programme (Baltic Regional Programme, BRP) was established in 1998. This programme covers a wide range of activities including agriculture, investment, labour, education, environment, etc. Within this programme, agriculture has been particularly active with a wide range of activities including the Policy Workshop in Parnu (1997), the Ministerial Meeting in Riga (1998), and the Dairy Workshop in Lithuania (2001).

- This brings me to this Seminar on agricultural incomes, labour mobility and rural development policies, which will take place over the next 2-3 days here in the conference centre of the Ministry of Agriculture, in this beautiful old town of Tallinn.

- As most of you will appreciate, this is a very complex set of issues covering a range of macroeconomic, regional, social and sectoral policies. In essence, the objective of this Seminar is to develop a better understanding of the underlying causes and linkages between these policies in the Baltic countries. In turn, this should help us to identify and design a set of approaches and policy instruments that could resolve these problems.

- The issue of low, volatile, and often declining farm or agricultural household incomes is a challenge faced by many countries. With increasing competition in the food sector and acceleration in the pace of structural change at the farm level, governments have responded to this challenge by introducing and implementing an array of programmes, many of which, although well intentioned, often fail to meet their initial objective. During this Seminar, several speakers will highlight how many of the current programmes for supporting farm incomes have been inefficient and ineffective in this regard.

- Associated with the income problem and the adoption of new technologies, is the issue of surplus labour, and the consequent outflow of labour from agriculture. Finding appropriate paths to facilitate labour adjustment in rural areas is another great challenge facing policy makers in all our countries.

- The third policy area that will be discussed during this Seminar is rural and regional development. This discussion will examine ways by which rural areas can be revitalised and greater employment opportunities provided for those on low incomes, unemployed, and/or leaving agriculture and other primary industries.

- For OECD, this Seminar is also quite unique and challenging. This is the first time that OECD has attempted to cover such a divergent range of topics that are not only very complex, but have implications that cross many policy frontiers. In getting a better understanding of the complex relationships between agricultural household incomes, labour mobility and rural/regional development policies should help to better inform policy makers in choosing between the different policy measures and approaches.

- I look forward to a very interesting and informed debate over the next 2-3 days. The reports from Estonia, Latvia and Lithuania, as well as from experts from OECD countries based on their experiences, will provide important insights into the linkages between these important policy areas. Moreover, these insights may help policy makers to develop the appropriate policy set or policy mix that raise incomes, lowers the rate of unemployment and accelerates economic development in rural areas.

In conclusion, ladies and gentlemen, on behalf of OECD, let me once again welcome all of you to this Seminar. To those, who are participating for the first time, I look forward to the fresh insights that your experience and research will bring to the debate.

SESSION 1. AN OVERVIEW OF THE AGRICULTURE AND RURAL INCOME SITUATION AND TRENDS IN THE COMPOSITION OF INCOME IN WESTERN EUROPE AND THE BALTIC STATES

A CONCEPTUAL FRAMEWORK FOR ESTIMATING AGRICULTURAL HOUSEHOLD INCOMES IN EU COUNTRIES

By Professor Berkeley Hill[1]

Abstract

Concepts relevant to income statistics for agricultural households are to be found within the internationally-accepted United Nations' System of National Accounts (SNA) and the EU version, the European System of Accounts (ESA). These were adapted by Eurostat for its Income of the Agricultural Households Sector (IAHS) statistics. Critical elements are the definitions of a household, what constitutes an agricultural household and the income concept used as an indicator. Enlargement of the EU will bring in countries whose agricultural structures include units that do not correspond to the traditional model of the private family farm; at one end of the size spectrum there are large enterprises that have their own legal status and, at the other, households with private plots that produce significant amounts of food. Both require a reassessment of the concept of the agricultural household and the measure of income. In all countries progress in generating results depends on the availability of suitable basic data.

Introduction

Agricultural production is not a disembodied activity, but is undertaken by households and other enterprises that have legal status. The way in which these real units respond to signals such as price movements and incentives for technical change determines their impact on production and this industry's structural adjustment. Understanding the economic situation of agricultural households is now recognised as a key element in designing and applying policy for agriculture and rural areas (Offutt 2002; OECD, 2002). Though, as will become evident, statistics for agricultural households are not fully developed, sufficient evidence exists to demonstrate the great policy relevance of this information (see the accompanying paper by Catherine Moreddu). Here the emphasis is on the methodological challenges these statistics face.

The structure of the agricultural industry of the EUR 15 is dominated, in terms of numbers, by firms owned and operated by households (household-firms).[2] These combine the economic functions of production and consumption and are, at the same time, social units. Their numbers have been in long-term decline as the treadmill of technology lowers the real prices of agricultural commodities and makes the smaller farms unviable (Eurostat, 2002).

However, a simplistic view of agricultural household-firms is both incorrect and harmful to the design of successful policy. They are highly diverse in many different dimensions. Attention is often focussed on the variety in size of their agricultural activities (land holdings, outputs, input uses etc.), farming types, performances, degrees of indebtedness and so on - all factors that will be reflected in

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1. Professor of Policy Analysis, University of London, and external expert to Eurostat 1986-2002 on its Income of the Agricultural Households Sector (IAHS) statistics.

2. According to the EU Survey of the Structure of Agricultural Holdings (Farm Structure Survey) "Natural persons" accounted for 98.8% of EUR 12 holdings in 1993. Only one country was below 97% - the UK at 93.7%.

the income levels from farming. But many households are also engaged in economic activities that are non-agricultural, either as waged employees (dependent activity) or as self-employed entrepreneurs (independent activity). While some non-agricultural activity may be sited on the farm, mostly this is off-farm. Households (and their members) also often receive other forms of income, from property (rents from land and interest and dividends from financial assets), social transfers (pension etc.) and other sources, though again the incidences of these income forms are far from uniform.

As a consequence, there is wide variation in the dependency of household-firms on agricultural activity, from 100% (with no non-agricultural income) to where farming represents only a minor income source, and in some cases a negative one (a loss). Even among households where agriculture is the main income source, or activity, there will be many that are diversified into non-agricultural activities. For farm-dependent households the policies directed at agriculture are of obvious importance, but for those toward the other end of the dependency spectrum the main influence will be what is happening to non-agricultural parts of the economy, and regional and rural development and policies. The wide variety of circumstances among farm households implies that a satisfactory measurement of their household income must go beyond the sector level, or group average, to include distributional information that reflects their diverse nature (Hill, 2000).

As will become apparent, behind current statistics for agricultural households (and many other statistics) lies the model of the family farm, in the form of a small or medium sized non-corporate agricultural business run on an entrepreneurial basis by people who also own all or some of the assets, and in which "income" is a residual profit. The (relatively few) family farms structured as corporations (companies) can be accommodated with little difficulty (often by assuming they are not incorporated). However the enlargement of the EU challenges this conventional view of what constitutes an agricultural household. The large-scale operations with their own legal status found in many countries that soon will be joining the EU, together with the many households there that produce for subsistence on private plots, present problems that, for agricultural households statistics, are not yet fully resolved. How they might be treated is reserved for a separate section later.

Activities and institutional units in the statistical system

A conceptual framework to economic statistics for agriculture, including those for agricultural households, is provided by the international standard System of National Accounts SNA93 (UN, 1993), interpreted locally as the European System of Accounts (ESA95)(Eurostat, 1996) and for agriculture generally by the FAO's System of Economic Accounts for Food and Agriculture (SEAFA96). Two main approaches to accounting, and the statistics derived from accounting, are given:

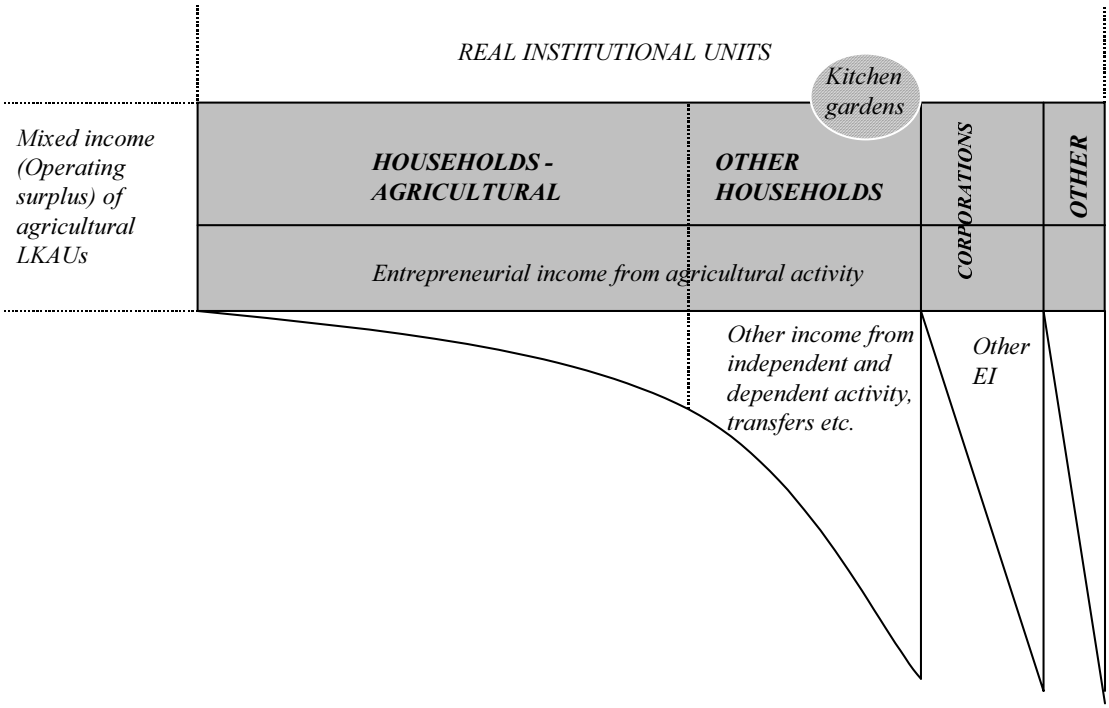
- Accounts for institutional units (households, companies, government etc.).
- Activity accounts for the production of goods and services, which may be broken up into agricultural activity and other types.

Of course, activity takes place within institutional units and, as these two approaches are part of a single system, they relate to each other. This relationship is shown in Figure 1, in which households appear as one form of institutional unit.

At present the main official indicators of agricultural income at aggregate and microeconomic levels in the EU are based on accounts that take the latter (activity) approach. The Economic Accounts for Agriculture (EAA) assumes an "industry" of fictional Local Kind of Activity Units (LKAUs) (Eurostat, 2000), while the microeconomic Farm Accountancy Data Network (FADN or RICA) uses

the concept of the "holding" shared with EU Farm Structure Survey.[3] Both levels are, essentially, only concerned with the activity of producing agricultural commodities; other (non-agricultural) forms of production and other economic activities are excluded (other than some that cannot be separated in the data sources). The preference for activity accounts is largely the result of historical factors (Hill 1998, 2000).

Figure 1. Relationship between household-firms, other institutional units and agricultural production (from Hill, 1999)



However, it is increasingly recognised that accounts relating to real institutional units (of which household-firms are numerically the most important) should be calculated, to stand beside existing activity-related indicators (for reasons outlined in Table 1). Eurostat has developed its Income of the

3. The EU's Farm Structure Survey defines the holding as "a single unit both technically and economically, which has single management and the output of which is agricultural products" (Eurostat, 1986). The legislation goes on to elaborate that a "single unit" is indicated by a common use of labour and means of production, and that formerly-independent holdings that come under a single management and single technical and economic unit should be treated as one holding. There is no condition of single ownership. Differing national legislation results in some variation in what is represented by the term "holding". In contrast with the technical and economic aspects of the EU approach, in some countries the "holding" is much more strongly linked to land and is not subject to explicit application of the single management criterion. For example, in the UK the holding is essentially a unit concerned with land occupation and affected by returning conventions in censuses, leading to a situation in which surveys in Great Britain have frequently found examples of several holdings being farmed together (Commission, 1981), that is, satisfying the conditions of a single management and technical unit but appearing in statistics as separate holdings.

Agricultural Households Sector (IAHS) statistics[4] to provide an aggregate (sector-level) picture (for the latest report and reference to earlier material see Eurostat, 2002). Though at present no official microeconomic agricultural statistics are in place, a number of Member States have national statistics. Agricultural households are covered in some general household statistics, including the EU network of household budget surveys and the EC Household Panel, though numbers are too small and/or data insufficiently robust to act as income statistics for agricultural policy purposes (Hill, 2000). The OECD has drawn on a number of these sources to present analyses of the income situation of agricultural households and to show the policy-relevance of this information (a synthesis of this work appearing as OECD, 2002).

Table 1. Characteristics of accounts based on fictional and institutional units

Accounts for fictional units (EAA LKAUs and FADN/RICA holdings)	**Accounts for real institutional units (agricultural household-firms)**
Strengths: Activity accounts have well established harmonised methodology, with tested data sources. EAA "industry" level - timely estimation by indirect methods. Surveys of microeconomic holding accounts provide disaggregated information (farm size, type etc.). Accepted widely by policy makers.	*Strengths* Relate to complete real institutional units, so avoids need to separate agricultural and other economic activities Integrated sequence of current and capital accounts and balance sheets. Better integration of sector and microeconomic (household level) statistics Easier interpretation by non-expert users. Direct relevance to policy aims. Better ability to explain behaviour of units Income indicators correspond with household's ability to consume and save.
Weaknesses Requires separation off of agricultural activity data from other activities undertaken by real units. Limited ability to explain producer behaviour. Difficult to interpret in relation to policy aims for the agricultural community. "Income" indicators do not correspond to resources available for consumption and saving at household level.	*Weaknesses* Definition of agricultural households varies according to use to which results are put. Data sources often not of good quality. Statistics not fully established at sector level, and not yet initiated at household level within agricultural statistics. Political and institutional caution towards results.

The SNA provides a methodological framework for statistics on household income. For institutional units this SNA lists a sequence of integrated accounts (current and capital) and balance sheets. Details are given in Annex 1. For households this sequence provides accounts for the entrepreneurial income generated from production, for all the resources flowing to households from income of all sorts, for the distribution of this total between what remains as disposable income once tax and other non-optional payments are made and, where data permit, the use of disposable income

4. At their inception in the mid-1980s these were termed Total Income of Agricultural Households (TIAH) statistics. The name change to IAHS statistics took place after the publication of the 1997 TIAH report in 1998.

for saving and consumption spending. Capital accounts and balance sheets are part of the series, the latter showing a net worth position.[5]

Defining agricultural households

Households that engage in agricultural activity do so at various levels and degrees of dependency. While for some, farming will constitute the prime source of income, for others, it will be a minor commercial activity, or perhaps production is only for domestic consumption or as a hobby.[6] Some means of distinguishing between the types of household is needed, in the present context this involves deciding what an agricultural household is (that is, settling on a definition, or range of definitions).

Several issues are involved; these were tackled as part of the methodology of Eurostat's IAHS statistics (Eurostat, 1995), but also have to be faced by alternative conceptual frameworks, such as household budget surveys. As will become evident, though general standards and recommendations are given in IAHS methodology, there is considerable flexibility for individual Member States to use variants that suit their particular data sources. The dangers flowing from the lack of strict harmonisation has to be offset against the advantage of having some results.

What is a household?

The IAHS definition of a household is as follows (Box 1):

Box 1. IAHS definition of a household

The household includes all members living together and includes, in agricultural households, both those who work on the agricultural holding and those who do not. (Eurostat, 1995)

The background to this is that ESA gives only a general indication of how a household should be defined. In the absence of an internationally applied definition of a household, the IAHS Manual of Methodology (Eurostat, 1995) states that the composition of households is to be defined as in the household budget surveys of Member States. This implies using the "dwelling unit" as the basis for drawing the boundary of the household. In practice, details vary between countries (*e.g.* the treatment of students away at university, or servants who share their employer's house). So does the treatment of communal units (such as religious houses) that are within the households sector according to the SNA/ESA definitions but that have a structure far removed from the typical farm household – for the purpose of Eurostat's IAHS statistics these should in theory be excluded.[7]

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5. For activities only some of this sequence can be drawn up. Strictly, these only include the *production account* (balancing item Net Value Added) and the *Generation of income account* (balancing item Mixed Income). The next in the series (*Entrepreneurial Income account* with its balancing item of *Entrepreneurial Income*) involves the deduction of interest paid and rent paid. These only relate to institutional units (households and companies). Under the EAA Entrepreneurial Income is estimated, but to link this with a agricultural activity requires assumptions about the relationship between the activity and the households (or corporations) that undertake production. These assumptions are increasingly unsafe.

6. The issue of what agricultural activity is covered in national accounts and in the separate satellite Economic Accounts for Agriculture is too large to cover here. Reference should be made to Eurostat, 2000 or Hill, 1996.

7. In some EU Member States, a small minority of family farms (typically the large ones) are arranged as companies, often for fiscal convenience. In reality, they remain family owned and operated, with a

In addition to the "dwelling unit", Eurostat has considered a definition of a "single budget" household that covers only those members of the "dwelling household" who pool income and expenditure (such as couples and dependent children) and excludes financially independent adults. In some countries extended households can be found in which many adult members (typically grown-up children living at home) have off-farm jobs and do not contribute their income to the common budget of the household-firm that operates the farm. In such circumstances the economic situation of the household-firm is (probably) better explained in terms of the income of a unit that excludes them. This "single budget" household may also correspond to the "fiscal household" used as the basis of taxation in some countries. However, because of lack of data, such a unit is not yet universally applicable within the EU. Consequently, attention is focussed on the "dwelling household". This also corresponds to the unit adopted in the EU network of microeconomic Family Budget Surveys; though different approaches are found, the unit applied in Member States usually conforms to the dwelling household (Verma and Gabiondo, 1993). In contrast, the EU Household Panel can, in theory, adopt a range of groupings, from the dwelling household downwards, because data are collected relating to individuals separately. This "variable geometry" for the household unit is not usually available in most datasets.

For use within income measurement it is necessary to know:

- The total number of households.
- The total number of household members:
    a. Number of persons.
    b. Number of consumer units.

The use of consumer units is a means for bringing households of differing compositions to a common base by attributing weights to various types of household member (for example couples, single persons, additional adults, children of various age bands). These weights are termed an equivalence scale; in IAHS statistics it is anticipated that, in the absence of contrary evidence, the scales used should be those applied in respective national household budget surveys.

What is an agricultural household?

The definition of an agricultural household chosen can make a substantial impact on both the number of households covered and the income picture that emerges (see, for example, results for Ireland described in Hill, 1988).

Criterion

The intuitive basis for classifying households as agricultural is that they are engaged in agricultural activity. What the agricultural community comprises and thus what it means to be "engaged" in agriculture has never been well defined by policy makers (Hill, 1990), and several interpretations are possible. For the purpose of IAHS statistics, households that work solely as employees on farms (hired workers engaging in dependent activity) are ***not*** considered to be agricultural households, a decision taken on the advice of the Agricultural Statistics Committee and which reflects both statistical practicality and the implied target group for support under the CAP is

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management structure similar to that of household-firms. Provision exists in the IAHS methodology for treating these as *quasi*-unincorporated units and including income results for them as an "add-on" to those for household-firms. (Eurostat, 1995)

targeted. This convention reflects the history of statistics and is under review in the light of EU enlargement (see Eurostat, 2002, and below). Thus currently in EU IAHS statistics, to qualify as an agricultural household there must be an involvement in income-generating independent productive activity in agriculture (self-employment as a farmer). A minimum threshold is applied to distinguish significant subsistence production (income in kind that may be considered a substitute for market output) from hobby activity.

Strictly, for a household to fall into the agricultural group there is no requirement that the household's own labour must be put into on-farm activity (a farm, owned by the household, could be operated entirely with hired labour), though in reality this will almost always be the situation.

Classification and dependency levels

For some purposes it may be necessary to present the income picture for all households that are engaged in independent agricultural production. This very broad coverage corresponds to the entire width of the household sector in Figure 1. It is similar to that used by the US in its reporting on its operator-households (Mishra *et al.,* 2002). The European Commission has indicated the desirability of having income statistics calculated on this basis, at least periodically.

However, for most situations a narrower coverage seems appropriate in which some households are screened out, leaving a coverage that is more relevant to the purpose for which the results are to be employed. Selection might include, for example, only those households responsible for levels of agricultural output or land area above given thresholds. Or it might include only those who were mainly dependent on farming for their income. The SNA recommends, as a general principle, that the purpose determines the way in which sub-sectoring is carried out.

A major objective of agricultural household statistics is to enable comparison to be made between the incomes of agricultural households and other socio-professional groups; this is important to ascertaining whether the EU policy aim of achieving a fair standard of living for the agricultural community is being attained. It follows that, for this purpose, agricultural and other household groups must be selected on a consistent basis, and this will be reflected in the chosen basis of classification. While it would be possible to compare the income situation of a group of agricultural households defined in a broad way with that of the all-households average (as is done in the USA), this would include many for whom agriculture is a very minor activity. There is greater validity in comparing households that are primarily dependent on agriculture with those that are primarily dependent on other income sources, such as those operating non-agricultural businesses, employees, pensioners and so on. Within the ESA such a disaggregation into socio-professional groups is allowed for and in which both gaps and overlaps are avoided (Box 2).

Box 2. ESA95 recommendations on methodology for subsectoring households

The ESA recommendation is that households are to be allocated to sub-sectors according to the largest income category (employers' income, compensation of employees, etc.) of the household as a whole. When more than one income of a given category is received within the same household, the classification must be based on the total household income within each category. (ESA 2.78). If the main income source of the household as a whole is not available for sectoring purposes, the income of the reference person constitutes the second-best characteristic to be used for classifying purposes. The reference person of a household is normally the person with the largest income. If the latter information is not available, the income of the person who states that he/she is the reference person may be used for sub-sectoring households (ESA 2.85). (Eurostat, 1996)

Building on these SNA/ESA guidelines, Eurostat's IAHS statistics methodology has defined an agricultural household for operational use in two ways (Box 3).

- For its **"broad" coverage** all households are included that derive some income from independent activity in agriculture (other than income solely in kind that is of a "hobby" nature). This income can arise from activity of the head of household or any other member.

- For its **"narrow" coverage** the IAHS applies a classification system based on the **main income source of the household's reference person** (Eurostat, 1995), a more practical approach than one that looks at the composition of the entire household's income. Thus a "narrow" agricultural household is one where the reference person's main income is from farming. This reference person is intended to be the household's highest income earner, who will also usually be the one regarded as the head of household. How this person is designated varies from country to country, and may be selected by self-declaration or more complex algorithms. Countries where an income-based classification is not feasible (*e.g.* France) have been allowed to apply a system based on the reference person's main *time allocation* or on a more subjectively determined occupation or trade group label. This alternative conforms with the approach taken to the allocation of households in the EU network of household budget surveys. It is recognised that some producers of significant volumes of agricultural commodities may be excluded from the "narrow" agricultural group if they have even larger incomes from elsewhere. Such exclusions may find political resistance.

The "narrow" definition takes precedence in the generation of IAHS statistics because it produces a group that appears to correspond more closely with the "agricultural community" whose incomes the CAP is intended to support. Of course, whichever definition is being used, the incomes of all household members are summed to achieve a total for the household.

Box 3. Definitions of agricultural households in Eurostat's IAHS statistics

An agricultural household ("narrow" definition) is one where the main income of the household reference person (typically the head of household) is from independent activity in agriculture (farming). A range of other socio-professional groups can be established on the same basis for the purpose of comparison. A second, supplementary, "broad" definition of an agricultural household includes all households where any member has some income from independent activity in agriculture. (Eurostat, 1995)

For the purpose of drawing income comparisons, IAHS statistics Eurostat has proposed a "minimum list" of socio-professional groups, of which agricultural households form one (the others being households headed by other self-employed people, by employees, by people dependent on welfare transfers including pensions, and a miscellaneous group).

Because incomes from agricultural production are inherently unstable, there is a danger that classifying according to income measured in a single year could cause substantial short-term variations in the size of the agricultural households sector. In turn, this has been found, in certain circumstances, to result in a movement in average household income that is perverse when compared to the pattern over time in the profitability of agricultural production (something exhibited by Denmark's early contributions to IAHS statistics). To avoid this, the use of stabilising mechanisms is encouraged, such as classifying households to groups on the basis of incomes averaged over (say) three years, or applying a more subjective judgement of "main income" over a run of years, or by reclassifying individual cases only periodically.

Subtracting the "narrow" coverage from the "broad" one results in a "marginal" group of households that engage in independent agricultural activity but where the main income is from some

other (non-agricultural) source. In the seven EU countries where this calculation is possible (though spread across several years) the “marginal” households are shown to be present in substantial quantities and in some countries are more numerous than “narrow” agricultural households (Table 2). Though highly heterogeneous, the “marginals” share the characteristic that agriculture is typically of little importance to them (for example generating only some 5% of household income in Germany in 1983 and 14% in Ireland in 1987: given in Eurostat, 2002 and earlier reports).

Table 2. Number of households and levels of average net disposable income for three groups of agricultural households, in selected EU countries

	Denmark (1999)	Germany (1983)	Greece (1994)	Ireland (1987)	Netherlands (1988)[1]	Finland (1992)	Sweden (1992)
			No. agricultural households (x 1 000)				
"broad"	57	613	615	207	136	139	94
"narrow"	16	353	398	85	87	73	54
"marginal"	41	260	217	122	49	65	41
			Disposable income per household (All households = 100)				
Agricultural households							
"broad"	99	110	114	105	210	124	81
"narrow"	105	101	86	127	267	131	79
"marginal"	92	123	166	89	108	116	85

Source: Eurostat (2002) reproduced from earlier reports.

Though attention has been concentrated here on households, a parallel classification of other institutional units (corporations etc.) might also be envisaged. In summation a picture could be presented of all units engaged in production, or for which it is the major activity (or similar subsets).

Defining income

The second key issue in methodology relating to income measurement of agricultural households is the definition of income to be adopted. The SNA/ESA provides a framework definition that covers all flows to and from the households sector; this can be adapted to apply at the sub-sector level (the agricultural households sector) by including flows to and from other households. In essence, this is the approach adopted by Eurostat in its IAHS statistics, in which the definition of income represents an amalgamation of five accounts in the SNA/ESA sequence; the *production account, generation of income account, entrepreneurial income account, allocation of primary income account,* and *secondary distribution of income account.* The balancing item is Net Disposable Income (NDI), the sum that is available for consumption spending (determining standard of living) and saving. An outline definition is given in Table 3.

It should be noted that this definition, taken from the methodology of national accounts, includes some elements that reflect its origins (in which all inter-sectoral transfers have to be recorded) and that would not normally appear in microeconomic data sources. Thus, while the main elements are common to both aggregate and microeconomic approaches, there will be differences in detail (Harrison, 1999). For example, household-level accounts would normally not show operating surplus; rather, they would show (entrepreneurial) income net of interest and rent payments, which in the IAHS formulation are deducted later in the series. Similarly, receipts from insurance claims would not

normally be seen as an income flow, and payment of insurance premiums would be regarded as an input cost in the same way as other purchases. Such differences should not be overstated; in Ireland they represent only about 15% of total household resource levels (Hill, 1995).

In reality, for generating IAHS statistics most Member States do not follow this national accounts definition exactly. Those using microeconomic data sources as the basis of their calculation (such farm accounts surveys or household budget surveys) typically omit items that are not available or that do not correspond with a more microeconomic approach to income measurement. For longitudinal analysis these omissions are not likely to be a severe handicap, though comparisons between countries are impeded. Thought has been given by Eurostat to the use of a simplified definition of disposable income that omits the more contentious items, thus achieving greater harmonisation between countries and, at the same time, provides an indicator that, arguable, is closer to the concept that policy makers have in mind when using the results.

Models for making calculations

Two main approaches are used to generate results at sector level (Eurostat, 1995). The first is to use microeconomic surveys which can be raised to national levels. These include household budget surveys, taxation records, surveys of farm accounts and other special surveys, either singly or in combination. Each type has its advantages and disadvantages (see Figure 4). For example, farm accounts surveys can be used where these collect data on the whole range of activities undertaken by the household; while their data relating to income from farming is generally good, their coverage of non-farm income of household members may be of lower quality and they will not contain data for other household socio-professional groups. Attempts to add questions on non-farm income to the official farm form of the EU's network of farm accounts surveys (FADN/RICA) to increase its utility to household statistics have met strong resistance (Robson, 1996). All surveys tend to be rather slow in generating results, which can only be available after data (usually retrospective) have been collected, checked and processed.

Countries differ widely in the availability and reliability of microeconomic data (Hill, 2000; OECD, 2002). Some (such as the Scandinavian countries) have several good datasets, several of which can be linked together (by means of personal identity numbers) to form a comprehensive database that can be interrogated for a variety of statistical purposes. On the other hand, some other countries do not have even one. For example, neither France nor the UK can at present provide microeconomic data on the overall income situation of their agricultural households that can be used to generate national estimates or to study the distribution of incomes.

Table 3. Definition of net disposable income (Eurostat IAHS statistics)

(1)	Net operating surplus (mixed income)[8] from independent activity
	a) From agricultural activity
	b) From non-agricultural activity
	c) From imputed rental value of owner-occupied dwellings
(2)	Wages (compensation to members of agricultural households as employees), from agricultural and non-agricultural activity
(3)	Property income received
(4)	Non-life insurance claims (personal and material damage)
(5)	Social benefits (other than Social benefits in kind)
(6)	Miscellaneous inward current transfers
(7)	Total resources (sum of 1 - 6)
(8)	Property income paid
(9)	Net non-life insurance premiums
(10)	Current taxes on income and wealth
(11)	Social contributions
(12)	Miscellaneous outgoing current transfers
(13)	**Net disposable income (7 minus 8 - 12)**
(14)	Social transfers in kind
(15)	Net adjusted disposable income (13 plus 14)

Notes for use of this definition in the context of microeconomic data sources:

1. Net operating surplus (Items 1a and 1b) is replaced by entrepreneurial income (that is, net of interest and rent payments related to production, and net of insurance premiums).
2. Net operating surplus from Imputed rental value of owner-occupied dwellings is often omitted.
3. Non-life insurance claims (receipts) are ignored – conceptually they form part of capital accounts.
4. Item 7 becomes Total Income.
5. Item 8 is blank, having been subsumed in Item 1a and 1b.
6. Miscellaneous outgoing current transfers do not include transfers that are deemed to include payments of a voluntary nature (such as to churches).
7. Items 13 and 14 are not covered.

8. Under the new SNA (1993)/ESA (1995), operating surplus and mixed income are alternative names for the same balancing item. Mixed income is the term used in the context of unincorporated enterprises owned by members of households in which the owners or other members of their households may work without receiving any wage or salary. Though farms are usually of this form, for the purpose of the TIAH methodology the term Operating surplus is used for this item; this is done to avoid potential confusion between mixed income and other microeconomic income concepts in which interest and rents have already been deducted.

Table 4. Three main forms of microeconomic agricultural household income data in EU Member States

Data source	*Advantages*	*Disadvantages*
Household budget surveys	• Agricultural households and other socio-professional groups are on a comparable basis	• Only periodic (typically 5 or 7 years) • Few agricultural cases in northern countries • Income data often of poor quality • Dwelling is not always the most appropriate unit
Taxation records	• Agricultural households and other socio-professional groups are on a comparable basis • Relative reliability of data	• Income concept reflects taxation conventions and coverage • Many farmers are not taxed on actual incomes, or escape the tax net • Difficult to obtain access to data
Farm accounts surveys	• Official harmonised system are already in place for monitoring farm incomes (FADN/RICA and the national surveys that contribute to it)	• In many countries these surveys do not cover income from outside the farm • Poor coverage of persons other than the farmer and spouse • Does not automatically generate figures for other socio-professional groups

The other main approach is to start from the households sector account within the national accounts, and to break them down into separate sub-sector accounts for a range of socio-professional groups, of which, agricultural households would be one. This is done using distribution agents taken from microeconomic data sources. These may be unsatisfactory as primary data but are more acceptable as a key to distributions (taxation data is often used in this way). Indirect estimates are also possible, such as developing a key for social benefits from knowing the age distribution of the population in agricultural and other households. The macroeconomic approach has the advantages of (a) building from the already-harmonised base of national accounts; (b) consistency of results with other economic aggregates; (c) generating comparable results for a range of other (non-agricultural) socio-professional groups, and (d) (often) better timeliness.

These two approaches can be used in combination. Each has its relative advantages and drawbacks. However, prime among these are that the microeconomic approach usually enables distributional information to be generated, while the macroeconomic starting point usually generates comparable figures for other socio-professional groups. Further discussion is given in Eurostat (1995).

Statistical issues of special relevance to countries in transition

EU Member States have been applying the IAHS methodology since the early 1990s, though France and Germany already had experience in making similar calculations within the framework of national accounts. The latest IAHS report (Eurostat, 2002) summarises the stage that each country has reached, and provides a detailed inventory of how they have interpreted and applied the methodology. Member States differ widely in the number of years for which results are available. For some

(including Denmark, Finland, Sweden and Austria) the calculation is now a regular annual exercise and a series is being established. However for others, figures relate to only a single year (Luxembourg), or there are other gaps, with little opportunity in the short term to make progress. The main restricting factor is not the methodology, but the availability of basic data by which to apply it. As noted previously, some countries do not have even a single satisfactory regular data source that covers the overall income of their agricultural households. At a time when statistical resources are under pressure, there is little ability to improve existing data systems and even less to set up new ones. Priority has been given elsewhere, such as updating the EAA. Consequently the flow of results is likely to be uneven, at least until such time as a strong political signal is given by policy makers of the utility of this information.

Some methodological developments under consideration to improve the quality of results have already been mentioned (the possibility of using a "single budget" household unit and a simplified measure of income). However, a major issue has arisen through the planned enlargement of the EU and the introduction of significant numbers of large scale-agricultural units that have their own legal status and that are far removed from the "family farm model" underlying IAHS statistics (and many others). Such units are already found in the unified Germany, but accession of Candidate Countries from 2004 will bring them into much greater prominence.[9] Replies to a Circular Note from Eurostat have shown that a range of organisational forms are encountered – agricultural enterprises arranged as joint stock companies, limited liability companies, co-operatives, partnerships etc., though in some countries with transitional economies the business structure is not yet stable. In at least some, the households that work on these large units are considered as part of the agricultural community and are seen as intended beneficiaries of agricultural policy. Furthermore, these households also commonly operate private plots that generate a significant share of their food supply and contribute a substantial proportion of the aggregate output of some commodities. However, such plots may also be operated by households that are not associated with large scale units.

There are implications for both the "narrow" and "broad" views of what constitutes an agricultural household, the statistical responses to which have not yet been fully worked out. As an interim, for the next version of the IAHS Manual of Methodology Eurostat has proposed to provide for the inclusion of income estimates for households found on large-scale enterprises as an "add-on", along the lines of the present provision for small companies that are operated and owned by single families (which are treated as *quasi*-agricultural household units) (see the 'future developments' section of Eurostat, 2002). This coverage will be additional to that of households operating private farms included by normal application of the existing target definitions. In the interest of simplicity and clarity, Eurostat is proposing that this new "add-on" should cover households working on ***all*** large-scale agricultural enterprises, irrespective of the form of legal structure that these units now take. To be included the household's reference person must work on a large agricultural unit and that job must be their principal occupation (in terms of income or, failing that, of time). It is assumed that this will be the case for most reference persons. At a future stage it will be necessary to clarify what constitutes a "large-scale agricultural unit", possibly using a size criterion. This issue is probably best handled at national level.

This "add-on" provision applies to statistics for agricultural households defined in the "narrow" way. The solution appropriate to the "broad" definition of an agricultural household is more problematic and needs further methodological consideration. While the "broad" coverage should obviously include the households of private farmers (deemed to be all those selling to the market and

9. For example, in Hungary, in 2000, corporate units constituted only 0.9% of numbers of farms but occupied 41% of the area.

thus generating some income from this activity) and of all workers on large units (to be consistent with the above treatment of reference persons found on them), the issue is complicated by the significant amounts of agricultural production of a subsistence nature that takes place on private plots.[10] This has been accommodated by a small proposed change in the Manual that includes within the "broad" definition households of subsistence producers, but excludes those of hobby producers, a distinction that is hard to make but which is intended to be consistent with the EAA. However, this solution on household classification should only be regarded as provisional. Another problem is posed by the valuation of the output from private plots and the contribution this makes to any measure of disposable income; though this issue is also faced by the EAA and national accounts, the solutions may differ (for example, valuation and retails or basic prices).

But perhaps the most significant issue in the development of income statistics for agricultural households is the availability of basic data from which the statistics can be built. As noted above, the situation varies widely between EU Member States. Setting up new data sources is highly expensive and generally ruled out. Thus the focus falls on better utilisation of what already exists ('adding value'), or of making marginal additions to established data collection systems. Though the prime candidate for development might seem to be European Commission's FADN/RICA system, attempts to expand the legal basis of its coverage to non-farm income (to enable it to approximate to income figures for the household of farmer and spouse) have met with political and institutional resistance (Robson, 1996). Another problem with this survey is that it applies a minimum size threshold (which varies between countries) that excludes many households that engage in agricultural production, even some that might satisfy the "narrow" definition of an agricultural household.

Solutions to this fundamental data problem have to be sought on a country-by-country basis. A necessary first step for countries joining the EU is to review existing information and data sources. There are many models that might be explored both among Member States (including farm accounts surveys in Austria, a combination of household budget and farm accounts surveys in Ireland, tax and other data assembled into an income statistics register in Finland) and elsewhere among OECD members (including the ARMS farms survey in the USA and tax filer data in Canada). In the past Eurostat has provided technical advice on this issue.

10. In 2001, in Estonia there were some 176 000 household plots (1.6% of agricultural area) in contrast with 85 300 agricultural holdings (98.4% or the area). Of the 32 400 ha occupied by household plots, averaging 0.18 ha, some 2 300 ha were used for potatoes.

ANNEX 1

The full sequence of accounts for households (SNA93 Table A.V.6)

I: Production account

Uses		Resources	
P.2	Intermediate consumption	P.1	Output
		P.11	Market output
		P.12	Output for own final use
B.1g	*Value added gross*		
K.1	Consumption of fixed capital		
B.1n	*Value added net*		

II: Distribution and use of income accounts

II.1: Primary distribution of income account

II.1.1: Generation of income account

Uses		Resources	
D.1	Compensation of employees	B.1	Value added
D.11	Wages and salaries		
D.12	Employers social contributions		
D.121	Employers' actual social contributions		
D.29	Employers' imputed social contributions		
D.29	Other taxes on production		
D.39	Other subsidies on production		
B.2	*Operating surplus*		
B.3	*Mixed income*		

II.1.2: Allocation of primary income account (which can be subdivided into two)

II.1.2.1 Entrepreneurial income account

Uses		Resources	
D.4	Property income (connected with market activities)	B.2	*Operating surplus*
D.41	Interest	B.3	*Mixed income*
D.45	Rent		
		D.4	Property income (connected with market activities)
		D.41	Interest
		D.42	Distributed income of corporations
		D.421	Dividends
		D.422	Withdrawals from income of quasi-corporations
		D.44	Property income attributed to insurance policyholders
B.4	*Entrepreneurial income*		

II.1.2.2: Allocation of other primary income account

Uses		Resources	
D.4	Property income (not connected with market activities)	B.4	*Entrepreneurial income*
D.41	Interest		
D.42	Rent	D.1	Compensation of employees
		D.11	Wages and salaries
		D.12	Employers' social contributions
		D.121	Employers' actual social contributions
		D.122	Employers' imputed social contributions
		D.4	Property income (not connected with market activities)
		D.41	Interest
		D.42	Distributed income of corporations
		D.421	Dividends
		D.422	Withdrawals from income of quasi-corporations
		D.43	Reinvested earnings on direct foreign investments
		D.44	Property income attributed to insurance policyholders
		D.45	Rent
B.5	*Balance of primary income*		

II.2: Secondary distribution of income account (simplified)

Uses		Resources	
D5	Current taxes on income, wealth etc.	B.5	*Balance of primary income*
D.61	Social contributions	D.61	Social contributions
D.611	Actual social contributions		
D.612	Imputed social contributions		
D.62	Social benefits other than social transfers in kind	D.62	Social benefits other than social transfers in kind
D.7	Other current transfers	D.7	Other current transfers
D.71	Net non-life insurance premiums	D.72	Non-life insurance claims
D.75	Miscellaneous current transfers	D.75	Miscellaneous current transfers
B.6	*Disposable income*		

II.3: Redistribution of income in kind account

Uses		Resources	
		B.6	*Disposable income*
		D.63	Social transfers in kind
		D.631	Social benefits in kind
		D.6311	Social security benefits, reimbursements
		D.6312	Other social security benefits in kind
		D.6313	Social assistance benefits in kind
		D.632	Transfers of individual non-market goods and services
B.7	*Adjusted disposable income*		

II.4: Use of income account

II.4.1: Use of disposable income account

Uses		Resources	
P.3	Final consumption expenditure	B.6	*Disposable income*
P.31	Individual consumption expenditure		
		D.8	Adjustment for the change in net equity of households on pension funds
B.8	*Saving*		

II.4.2: Use of adjusted disposable income account

Uses		Resources	
P.3	Actual final consumption	B.6	*Adjusted disposable income*
P.31	Actual individual consumption		
		D.8	Adjustment for the change in net equity of households on pension funds
B.8	*Saving*		

III: Accumulation accounts

III.1: Capital account (simplified)

Changes in assets		Changes in liabilities and net worth	
P.51	Gross fixed capital formation	B.8n	*Saving, net*
K.1	Consumption of fixed capital	D.9	Capital transfers, receivable
		D.92	Investment grants
P.52	Changes in inventories	D.99	Other capital transfers
P.53	Acquisitions less disposals of valuables		
		D.9	Capital transfers, payable
K.2	Acquisitions less disposable of non-produced non-financial assets (land etc.)	D.91	Capital taxes, payable
		D.99	Other capital transfers, payable
B.9	*Net lending / borrowing*	B.10.1	*Changes in net worth due to saving and capital transfers (Total of the above)*

The other accounts (not detailed here are as follows)

III.2: Financial account

III.3: Other changes in assets accounts
- III.3.1: Other changes in volume of assets account
- III.3.2: Revaluation account
  - III.3.2.1: Neutral holding gains/losses account
  - III.3.2.2: Real holding gains/losses account

IV: Balance sheets

IV.1: Opening balance sheet
IV.2: Changes in balance sheet (within which the change in net worth is attributed to savings and capital transfers, other changes in volume of assets, and nominal holding gains/losses)
IV.3: Closing balance sheet

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FARM HOUSEHOLD INCOME SITUATION IN OECD COUNTRIES: POLICY IMPLICATIONS

By Ms. Catherine Moreddu

Abstract

Concerns about the level, variability and distribution of farm household income are prominent in most OECD countries. Available information shows that although the ***income levels*** *of farm household in most OECD countries are, on average, close to those in the rest of society, there is a higher incidence of low income among farm households and there are* ***disparities*** *by farm size, type and region. However, if income* ***variability*** *can be a problem at the individual level, this does not appear to be the case at the aggregate national level because government intervention and the diversification to off-farm sources of income have reduced annual variations.*

In most OECD countries, large amounts of support are transferred to producers, thereby raising average farm household income to some extent and reducing income variability. This comes, however, at a very high cost. The main problems relate to ***targeting*** *– the bulk of the measures are generic in nature and go to farm households who do not need it; to* ***equity*** *– because measures are predominantly based on production or factors of production they fail to change income distribution in any significant way; and to* ***leakages*** *– much of the support is transferred to unintended beneficiaries. Yet, from an income transfer efficiency point of view, budgetary payments decoupled from agricultural activity altogether would transfer income to selected farm households more efficiently.*

Why are there still concerns for the incomes of farm households?

Although the scope of objectives attributed to agricultural policies has broadened, income objectives are still prominent in many OECD countries. Governments support the agricultural sector, often through large transfers, to improve these levels, to alleviate the incidence of low income and to reduce income variability.

Governments justify such intervention on grounds of ***market failure*** (and therefore ***efficiency***), in particular with respect to risk management, and ***equity***. The risk management rationale assumes that, in the absence or incompleteness of contingency markets,[1] uncertainties affect producers' decisions regarding production and the use of resources, and lead them to produce below the level of output that would maximise profit in the absence of risk. Risk reduction measures, and safety net measures protecting farmers against downside risks, can thus be envisaged to avoid market failure. Regarding equity concerns, sector-wide income support was introduced at a time when rural areas and farm households were lagging, but there is a need to re-evaluate the income situation of farm households, both in terms of aggregate level and the incidence of low income. In fact, concerns about income disparities within agriculture have increased as policy transfers become more visible and remain largely linked to production levels, and as production becomes more concentrated.

This paper aims to gather evidence in order to assess whether the belief that farm households need to be supported on income grounds still holds and whether current policies are efficient in

1. Examples of contingency markets are futures markets, options, insurance markets, the bond market and the stock market.

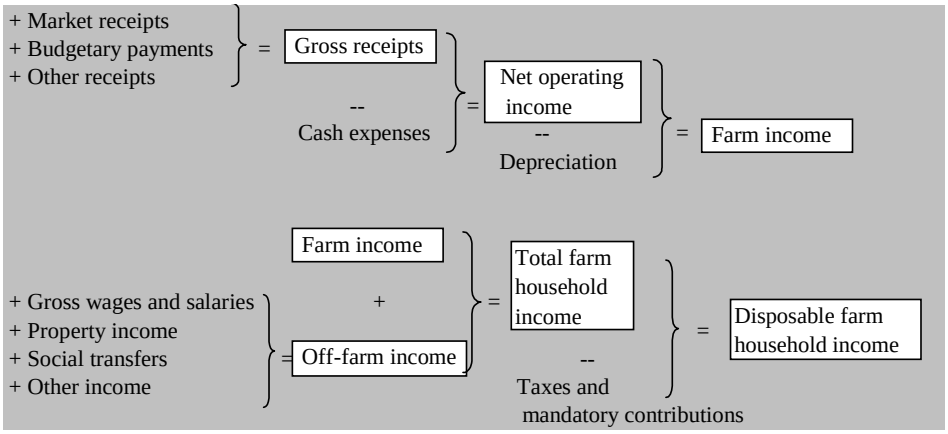
pursuing stated income objectives. This exercise is part of a mandate given by OECD Ministers to assess current support policies, not only in terms of their effectiveness and efficiency to achieve their objectives, but also in terms of operational criteria such as targeting and equity (OECD, 1998).

This paper is based on a recent publication (OECD, 2003*a*) that brings together and updates various OECD analyses[2] to produce a comprehensive study of farm household income issues in OECD countries. The following sections review the income situation of farm households in OECD countries for which data are available, and examines the role that agricultural policies, whatever their objectives, have played in determining the observed outcomes. Finally, policy solutions are proposed that would improve farm household income more effectively and equitably.

What is the income situation of farm households?

The situation presented here is one that emerges from national statistics; Measurement issues are discussed briefly in Box 1 and at greater length in Hill (2003). Farm household income is the indicator chosen to reflect the income situation of farm households. It includes farm income, defined as net income from farming activities, and income from non-farm activities, investments, social transfers and other sources (Diagram 1).

Diagram 1. Components of farm household income



2. OECD, 1995*a*, 1995*b*, 1995*c*, 1995*d*, 1996, 1999*a*, 2000, 2001 and 2002.

Box 1. Definition and measurement issues

What is the appropriate indicator to measure the income situation of farm households? Farm income provides only a very partial view of the income situation of a farm household. In order to reflect the income situation of farm households, all sources of income should be taken into account (Diagram 1). For a full assessment of the economic situation of farm families, farm and household assets should also be considered in combination with income, but because of data and resource constraints, the present study focuses on the income situation of farm households. [3]

Is the appropriate information widely available? Another problem concerns availability, quality and access to relevant data. Do the data collected in OECD countries allow progress towards income objectives to be systematically and accurately measured? For many countries the answer is no. In some cases the data are seriously out of date. Additional difficulties are created by the fact that in many countries the definitions adopted for households, income, etc., are too narrow to allow the real income status of farm households to be evaluated. The number of farm households in economy-wide income surveys is often too small to be representative, which makes it difficult to compare the situation of farm households with that of other households. Finally, farm household income can be underestimated. Income in-kind is often not taken into account and there can be problems linked to confidentiality and asymmetric information with reporting income in surveys. Farm self-employment income, in particular, might not be fully captured.

Are data comparable across countries? In general***, they are not***. First, the definition of farm households varies both with respect to who constitutes a household (which family members) and with respect to what constitutes a farm household (what level of sales, amount of land farmed, share of income from farming or other indicator qualifies a household as a farm household). There are enormous differences among countries with respect to these variables. Second, there are differences in the indicators of income that are reported, although with detailed information on farm accounts a common definition of farm income can be adopted. The coverage of income sources often differs. In particular, there are still many countries in which off-farm sources of income of farm households are not reported. For these reasons, comparisons across countries have not been attempted in this report. For each country where data are available, income components are compared between farm and non-farm sectors and across various groups in the agricultural sector.

What was used in this analysis? Macroeconomic accounts of the agricultural sector provide an aggregate measure of farm income (OECD, 1999*b*). In most cases, these data do not include non-agricultural income. A EUROSTAT project collects macroeconomic data on the total income of agricultural households for European Union (EU) member countries (EUROSTAT, 1999 and 2002) and was used in this report for some countries. However, they often refer to a narrow definition of farm households (main occupation farms of a minimum size for example). Consequently, whenever possible, national statistics that define farm households more broadly are used, in order to give a wider picture of the sector. With national account/macroeconomic data, the level and composition of the total income of farm households can be examined and compared to that of other sectors.

To look at the distribution of income or the incidence of low income among farm households compared to other households, at the change in income over time, and the impact of agricultural, social and taxation policies, microeconomic data were used. They either come from specific surveys (farm, household expenditure, or income surveys), or from tax and social transfers files. Economy-wide surveys allow comparison between farm households and other households. In many cases, however, the sample of farm households proves to be too small to allow a detailed and representative distributional analysis. The LIS (Luxembourg Income Study), which contains micro data from national household surveys, allows such a comparison for at least some countries and has been used in the analysis of the incidence of low income in different categories of households reported in OECD (2001) and summarised in this paper. Specific farm surveys provide useful structural information on farm households, allowing the income situation to be related to structural characteristics, but they do not permit direct comparison with other households (unless linked with an economy-wide survey). The OECD structural database, which has been used to analyse the impact of support on the distribution of income, contains such data.

Issues related to farm household income data availability and quality are not just, or even primarily, of interest to analysts. The principal beneficiaries of improved information would be policy makers and the public they serve. Until the coverage, timeliness and consistency of national microeconomic data is improved, policy measures, ostensibly aimed at improving the incomes of farm households, will be implemented without adequate knowledge of the nature, incidence or even existence of the problem that they are attempting to solve.

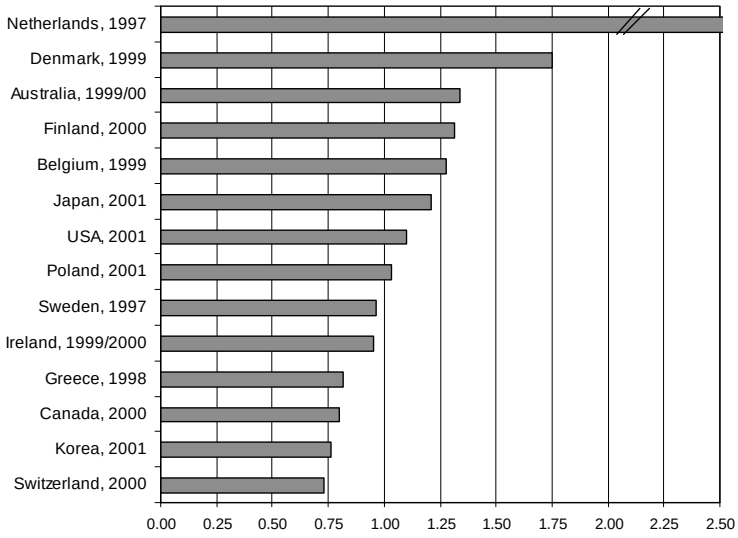
3. Box 1 in OECD (2003*a*) discusses briefly the issue of wealth. Farm families, who own part or all of the factors of production farmed, usually own considerable wealth, even when their income is low. The net worth of farm households is usually more equally distributed than their total income. Little is known about the non-farm assets of farm households.

How do the incomes of farm households compare on average with those in the rest of society?

In most OECD countries for which data are available, the average income of farm households is close to the economy-wide average (Graph 1). For the average of the three most recent years, farm household incomes are significantly higher (by over 15%) in the Netherlands, Denmark, France, Finland and Belgium, and significantly lower (by over 15%) in Greece, Korea, Turkey and Switzerland.[4] These results confirm the findings of prior OECD work (OECD, 1995*b* and 1998).

Graph 1. Total income of farm households as a ratio of that of all/other households

(most recent year available)



All households except for Japan, where it is workers' households and Korea, where it is urban households.
Source: Secretariat's calculation based on national statistics and EUROSTAT database (EUROSTAT, 1999 and 2002). Update from OECD (2003*a*).

What are the sources of farm household income? How important is agricultural income?

Farm households derive a significant share of income from off-farm sources (Graph 2), even when a very restrictive definition[5] of farm households is adopted. Where a broad definition is adopted, farm income is not even the main source, reflecting the diversity of farm households, which include pluriactive, pension or hobby farm households.

Regardless of definition, wages and salaries were the main source of off-farm income in three-quarters of the countries examined. Often, the farm operator himself is employed outside the farm, but increasingly the spouse may also have off-farm employment. Cases where social transfers

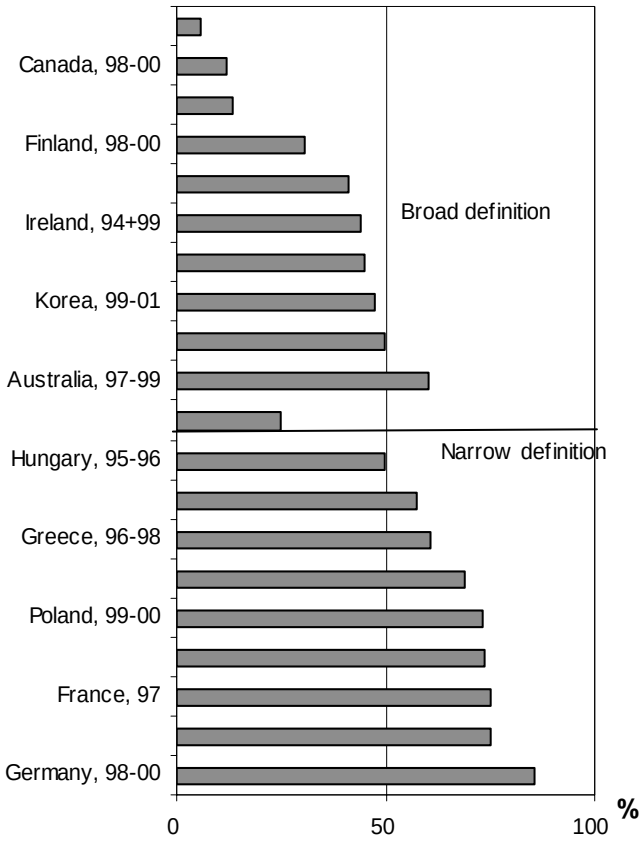
4. It should be noted that some of the data in Graph 1 are dated.

5. A more restrictive definition involves the exclusion of smaller farms (based on gross sales or area) and part-time farmers, for whom farm income is not the main source of income or agricultural activity is not the main activity.

are higher than salaries and wages are found in countries which restrict the definition of a farm household to the operator, whose main occupation is farming, and the spouse. Finally, property income is the primary source of off-farm income in the United Kingdom only, but comes next in importance in close to a third of the cases reviewed. These results do not generally depend on the year chosen.

Graph 2. Percentage share of farm income in total income of farm households

(average of the three most recent years available)



1. Income from independent activities.
2. Agricultural households in rural areas.
Source: Secretariat's calculation based on national statistics and EUROSTAT database (EUROSTAT, 1999 and 2002). Update from OECD (2003*a*).

How stable are farm household incomes?

Agricultural activity is subject to different risks, some natural or biological in origin, others economic. These risks affect production volumes and prices, and are thought to result in receipts and incomes that are more variable than in many other sectors. Farmers thus adopt strategies to reduce the variability of their total income.[6] A number of market-based tools are at their disposal, like

6. These strategies are reviewed in OECD (2000).

diversification of income sources, capital and debt management, marketing techniques, hedging on futures markets and insurance. In most countries, agricultural, social and fiscal policies, whatever their objective, also shield farm households against large losses of income (see section on policy impacts).

As a result, aggregate farm income at the national level does not appear to exhibit strong variability. At the individual level, excessive farm income variability can, however, be a problem, in particular for farms that have not been able to adopt basic income risk strategies and, as a result, are too dependent on one source of income or do not have sufficient savings or capital raising capacity. Because of the stabilising effect of non-farm income, total farm household income is often more stable than farm income and is generally not significantly more variable than that of other households (Table 1).

Table 1. Income variability in selected OECD countries

(in national currency, deflated by the GDP deflator, 1995=100)

Coefficient of variation [1]	Australia	Canada	Denmark	Japan	Norway	United Kingdom	United States
over the period	1989-99	1989-97	1989-99	1990-2001	1989-99	1988-99	1991-00
Farm income	0.49	0.26	0.16	0.12	0.14	0.17	0.28
Total income of farm households	0.31	0.05	0.08	0.02	0.06	0.08	0.14
Total income of all households [2]	0.12	0.03	n.a.	0.02	n.a.	n.a.	0.09

n.a.: not available.
See Diagram 1 for a definition of income indicators.
1. The coefficient of variation is the standard deviation divided by the average for the period.
2. Except for Japan, where it is workers' households.
Source: Secretariat's calculations based on national statistics; GDP deflator from OECD *National Accounts* database. Update from OECD (2003*a*).

How large are income disparities?

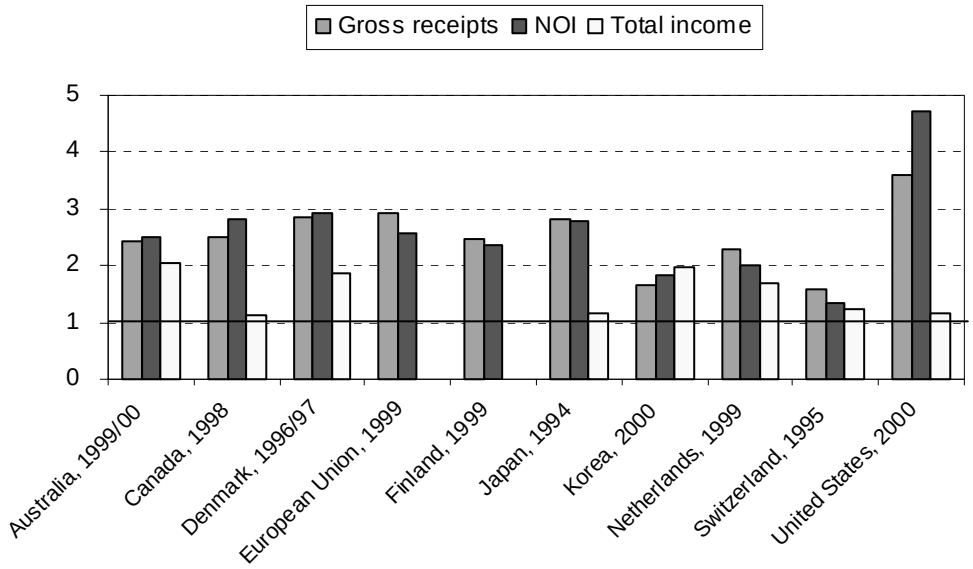
Many factors such as region, the structural characteristics of the farm and the household, and the economic environment, in particular the opportunities for off-farm earnings, affect the total income of farm households. Differences in average income by farm size and farm type in selected OECD countries, based on structural farm account data, are presented here.[7] In most countries reviewed, the average net operating income (NOI)[8] of farms in the top quartile[9] is two to three times bigger than that of all farms (Graph 3). The exceptions are Switzerland, where farm income inequalities are smaller, and the United States, where they are much larger. In all cases, the distribution of income reflects that of gross receipts, which, in part, depends on the definition of farms included in survey data. The distribution has been truncated when minimum limits on farmland, the value of commercial sales, or the share of income from farming or time spent on farming activities are placed on survey farms (as is the case for Swiss data).

7. See OECD (1999*a*) for a description of the characteristics of national farm account data. Whenever possible, the analysis reported here has been updated to most recent data available.

8. See Diagram 1 for a definition of income indicators.

9. The top quartile contains the 25% largest farms, based on gross sales.

Graph 3. Average gross receipts, net operating farm income and total income of the top quartile (25% largest farms) as a ratio of the average of all farms



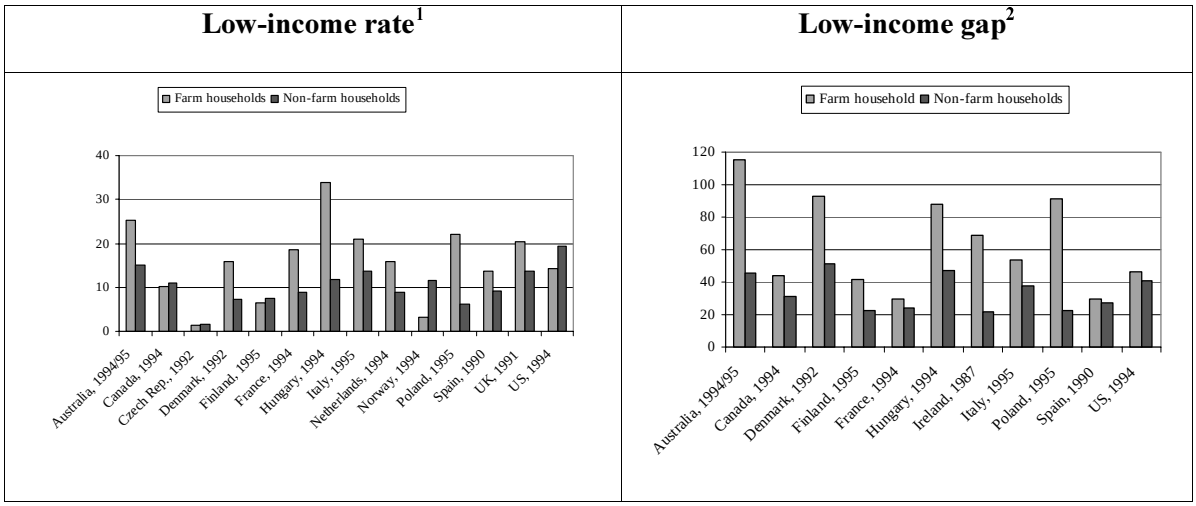
NOI: Net operating income. See Diagram 1 for a definition of income indicators.
Source: OECD structural database (OECD, 2003*a*).

Owing to differences in farm size, in productivity and in levels of support between commodities, there are also income disparities between farm types although they are not as large as between farms classified by gross sales (OECD, 2003*a*). Similarly, there are income differences by region, which stem from regional variations in the economic size of farms, type of farming and rate of support for each commodity, and how widely regions are defined. These issues were briefly examined in OECD (1999*a*). In all cases, when non-agricultural incomes are taken into account, differences in income by farm size, type and region are reduced.

Is low income more pervasive among farm households than in the rest of society?

In many countries, available evidence suggests that in the mid-1990s the incidence of low income was higher among farm households than among non-farm households. The low-income rate (defined in note 1 of Graph 4) was higher for farm households than non-farm households in 9 out of 14 countries, slightly lower in three (Canada, the Czech Republic and Finland), but significantly better in two (Norway and the United States) (Graph 4). The low-income gap was bigger for farm than for non-farm households in all the examined countries (note 2 of Graph 4). When the analysis is repeated using a narrow definition of the farm household, inequality is greater (OECD, 2001). In other words, farm households which rely more on farm activities are more frequently included in the low-income category. This confirms the importance of off-farm activities.

Graph 4. Low-income rate and low income gap: farm versus non-farm households



1. The low-income rate is the share of individual farm households with incomes falling below the low-income line (50% of median income of all households).
2. The low-income gap is the difference between the average income of the low-income farm households and the low-income line (the average income gap).

Source: OECD, 2001 (LIS data).

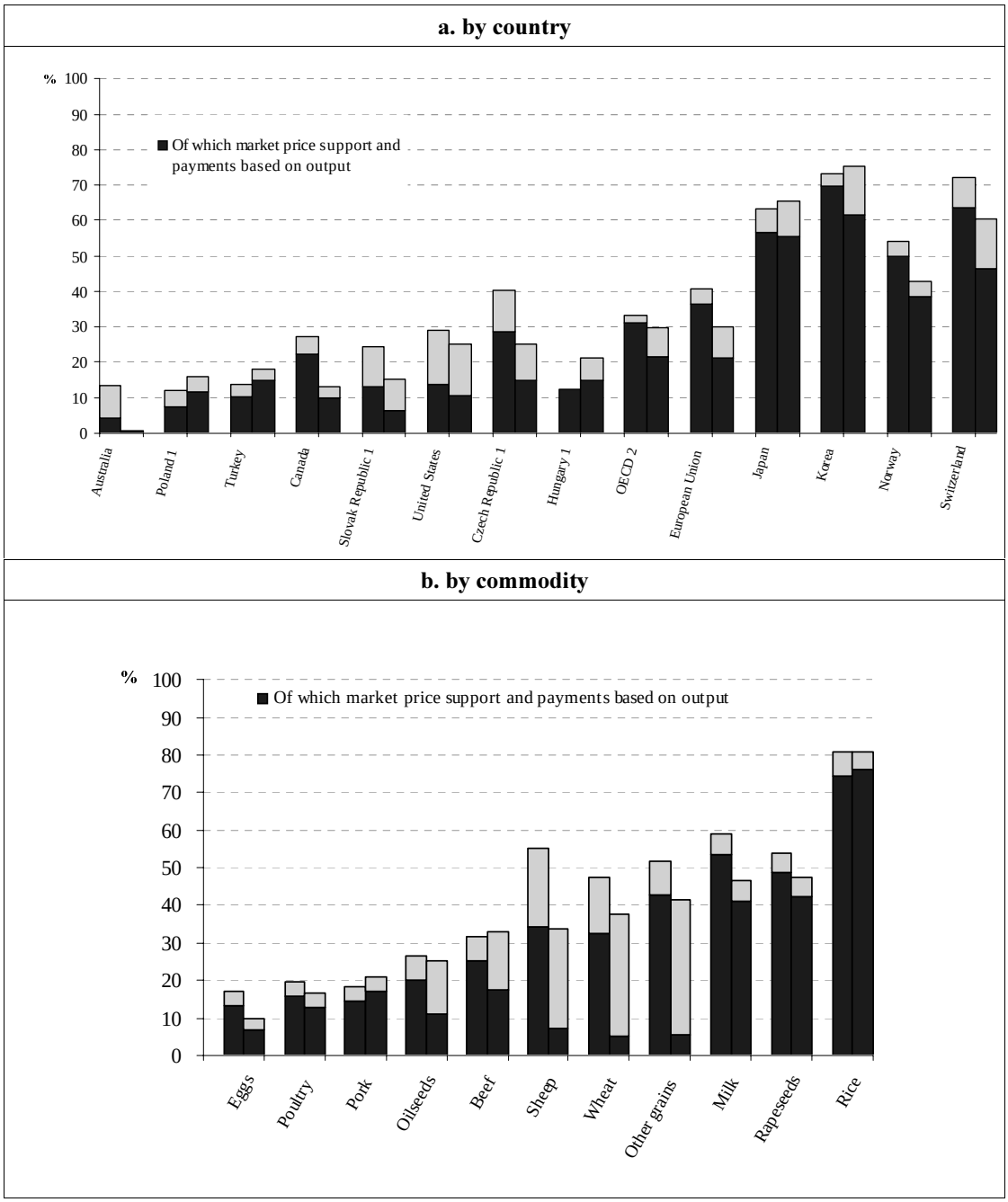
What is the impact of fiscal, social and agricultural support policies on farm household income?

How important is government support in farm income?

The Producer Support Estimate (PSE) expressed as a percentage of gross receipts explains, in static terms, the share of gross receipts that comes from government support (Graph 5). For example, in the OECD area, one third of gross receipts resulted from support in 2000-02 (OECD, 2003*b*). We cannot deduce from the PSE, however, that farm household incomes would fall by an equivalent percentage if all government support was removed given that in the absence of support, adjustments would occur. In addition, a large share of the transfers generated by agricultural policy and included in the PSE does not necessarily translate into net income gains for farm households. There are two sources of transfer losses that limit the income transfer efficiency of policy measures. The first is economic costs, which result from distortions in the use of resources and its incidence on production and trade patterns. The second source of loss is distributive leakages, whereby some of the benefits of support accrue to groups other than the intended beneficiaries. This latter category includes the costs of administering farm programmes, the extra payments that farmers are required to make to input suppliers or downstream industries, additional payments to landlords and income transfers to (or from) other countries.

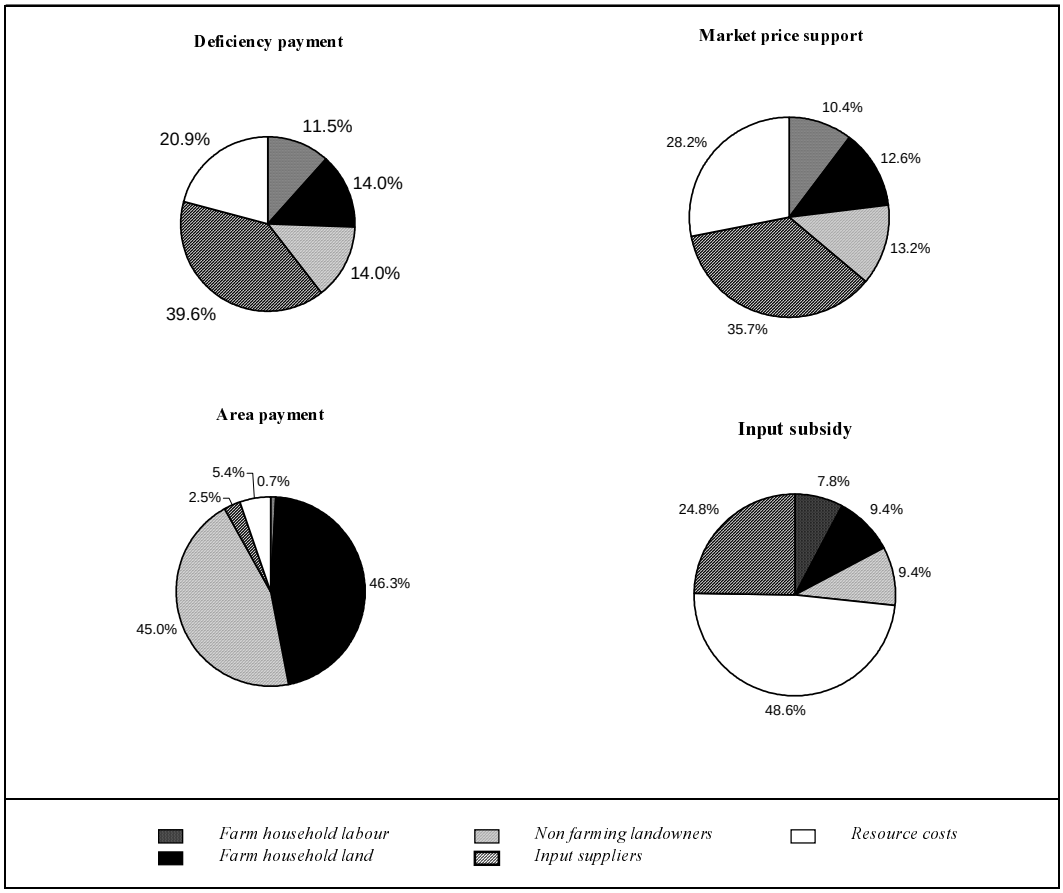
According to OECD estimates of income transfer efficiency, no support policy linked to agricultural activity succeeds in delivering more than half the monetary transfers from consumers and taxpayers as additional income to farm households. In the case of market price support and deficiency payments, the share is one fourth or less, and for input subsidies it is less than one-fifth (Graph 6).

Graph 5. Producer Support Estimate as a percentage of gross receipts, by country and by commodity, 2000-02



For each country and each commodity, the first bar corresponds to 1986-88 and the second to 1999-2001
1. For the Czech Republic, Hungary, Poland and Slovakia, 1986-88 is replaced by 1991-93.
2. For 1996-88, the Czech Republic, Hungary, Poland and Slovakia are excluded.
Source: OECD PSE/CSE database (OECD, 2003*b*).

Graph 6. Where does the money go? The income transfer efficiency of agricultural support



Source: OECD, 2002 and 2003*a*.

In the case of market price support and deficiency payments, the stimulus to output, and hence to input demand, means that much of the increase in receipts is paid back to input suppliers or capitalised into land values. Not surprisingly, input suppliers reap most of the benefits of input subsidies. In the case of area payments, nearly all the benefits are absorbed in increased land values.

What is the impact of agricultural policy on income risk and income variability?

Government intervention affects income risk for farm households at different levels (OECD, 2000). In addition to providing a stable economic environment and social safety nets for all households, governments in many OECD countries support their agricultural sector. Whatever their objective, many agricultural policy measures affect risk either by reducing farm income variability by stabilising input and output prices and quantities, or by raising income level and therefore modifying the attitude of farmers towards risk.

For almost all the countries and crops considered, a static analysis of variability over the period 1986-2000 has shown that almost all PSE categories of support contribute to reducing the variability of farm receipts (OECD, 2003*a*). The reduction in the variability of receipts due to support measures can be as high as 72% as in the case of wheat in the European Union. In countries with low levels of support, the impact is very small but there is, in general, no proportionality between the level of

support and the reduction in receipt variability. In most countries and for most commodities, the total reduction in receipts variability is mainly explained by the impact of market price support, reflecting the lack of price transmission between the world markets and domestic markets, especially in countries using explicit border mechanisms to isolate domestic markets (*e.g.* European Union, Japan, Korea, Norway and Switzerland). In other countries, various types of budgetary payments also play a significant role in reducing farm receipts variability, either in addition to market price support (Norway and Switzerland), or alone (Canada and the United States).

What is the distributional impact of support?

The static comparison between the distribution of support and that of gross receipts indicates the direction of the impact support has on the distribution of income.[10] Distributions by farm size, farm type and region have been examined for selected countries. Using the same methodology as in OECD (1999*a*), the distribution of gross receipts, support and income by farm size is compared in Table 2 using Gini coefficients[11] and graphically in Graph 7, which shows the share of the 25% largest farms in gross receipts, support and income.

Table 2. Gini coefficients

	Australia	Canada	Denmark	European Union	Finland	Japan	Korea	Netherlands	Switzerland	United States
Year	1999/2000	1998	1996/97	1999	1999	1994	1999	1999	1995	2000
Gross receipts [1]	0.59	0.61	0.74	0.73	0.64	0.70	0.32	0.54	0.27	0.91
Market price support (MPS) [2]	0.48	0.88	0.75	0.78	0.73	0.67	0.31	0.52	0.03	0.99
Direct payments (DP) [3]	n.a.	0.33	0.55	0.54	0.54	0.66	0.10	0.00	0.34	0.83
Total support (MPS + DP)	0.48	0.75	0.67	0.70	0.61	0.67	0.31	0.50	0.27	0.88
Net operating income	0.66	0.76	0.09	0.64	0.62	0.71	0.42	0.47	0.18	n.c.
Farm income	n.a.	n.c.	0.84	0.62	0.62	0.78	0.50	0.58	0.17	n.c.
Total income	0.44	0.02	0.33	n.a.	n.a.	0.07	0.46	0.32	0.13	0.03

n.a.: not available. n.c.: not computable because of negative averages for some quartiles.
See Diagram 1 for a definition of income indicators.

The Gini coefficient (Ig) is calculated as $Ig = \frac{\sum_i \sum_j | x_i - x_j |}{2n(n-1)x_m}$ for i = 1 to n and j = 1 to n

where x_i and x_j are the average of group i and group j respectively, and x_m is the average of the whole population. The greater the inequality, the higher the coefficient. When based on individual data and when all observations are positive, the Gini coefficient ranges from 0 to 1.

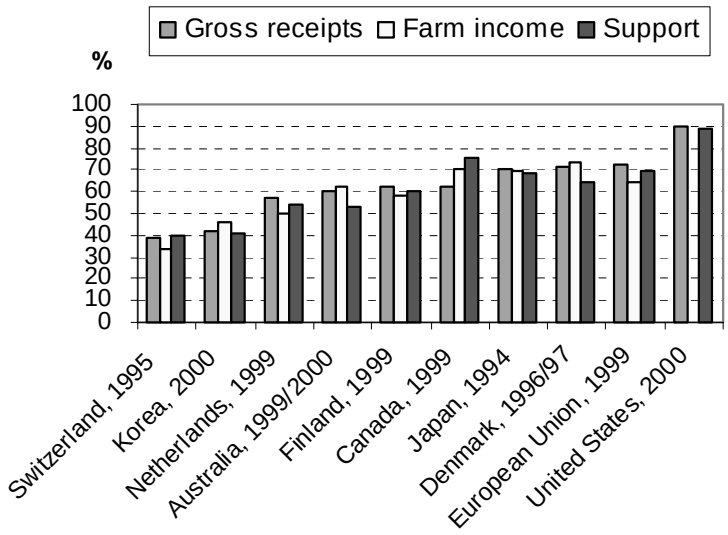
1. Gross receipts are the sum of receipts from sales of crop and livestock products, direct payments, receipts from agricultural activities off the farm and, in some countries, on-farm use.
2. Market price support is calculated by applying the ratio of market price support to the total value of gross receipts to receipts of each commodity for which an individual market price support is calculated in the PSE database and by applying an average ratio of all PSE commodities to remaining receipts.
3. Direct payments are budgetary transfers to farmers from agricultural policy. In the case of the European Union, subsidies for intermediate consumption are included.

Source: OECD structural database (OECD, 2003*a*).

10. It should be noted that support is included in the value of gross receipts.

11. See Note at the end of the main report for a definition of Gini coefficients. It should be noted that when based on group averages, as here, the Gini coefficient is undervalued, especially since there are very few groups. The Gini coefficients used in this report and based on quartiles should therefore be viewed only in relative terms, between variables for the same country.

Graph 7. Share of the 25% largest farms in:



Source: OECD structural database.

The distribution of support by farm size is similar to the distribution of gross receipts. This is because a large share of support in the OECD area is linked to the level of production[12] or the level of input,[13] and also because in many cases, support accounts for a significant share of gross receipts. The largest farms, and often the most prosperous ones, are therefore the main beneficiaries. Graph 7 shows that the 25% largest farms receive between 40 and 90% of support. In this sense, support is inequitable. On average, direct payments are more equally distributed than market price support and gross receipts, but the difference is generally small. Among EU member countries, a notable exception is the Netherlands where direct payments are equally distributed because many of the larger farms are specialised in horticulture which receives little in the way of CAP payments. This also explains why the level of payments received by Dutch farmers is low. In Switzerland, direct payments are also relatively equally distributed as their attribution is subject to many constraints related to size and farming conditions. We can conclude overall that, in most countries, support has a rather small redistributional effect by farm size because it is only slightly less unequally distributed than gross receipts. Exceptions are Canada, where support is more unequally distributed than gross receipts because dairy farms, which on average receive eight times more support than the average of all farms, are concentrated in the largest quartile, and Switzerland, where support has the same distribution as gross receipts (1995 data).

The impact of support on income disparities by farm type depends on how wide differences in support level are in the country and on how narrowly farm types have been defined. In the European Union, for example, support has widened disparities between dairy and intensive livestock farms on the one hand and field crop and cattle farms on the other. There are, nonetheless, a few cases where

12. Close to seventy per cent of the PSE in the OECD area came from market price support measures and payments based on output in 2000-02 (OECD, 2003*b*).

13. In 2000-02, payments based on area planted or animal numbers and payments based on input use accounted respectively for 13 and 9% of the PSE for the OECD area (OECD, 2003*b*).

support narrows disparities but the effect is relatively small. Overall, support increases income disparities between farm types (Graph 14 in OECD, 2003*a*).

There are also regional differences in the distribution of support. While support linked to output automatically goes to larger farms, direct payments can be targeted to less favoured areas. Although this is done to some extent in Switzerland, inequality nonetheless persists despite these efforts (OECD, 1999*a*).

What is the impact of taxation and social policies on the relative income situation of farm households?

Many countries grant preferential tax arrangements to farmers (*e.g.* Australia, Czech Republic, Hungary, Mexico, Norway, Sweden and the United States).[14] In Australia and Sweden for example, the purpose of the concession is to smooth income over a number of years and therefore help farmers deal with income risk. Available evidence suggests that in many countries, the situation of farm households relative to other households improves after taxes are deducted *i.e.* when disposable income is used for comparison rather than total income (OECD, 1995*b* and 2003*a*). Indeed, in the majority of countries examined, the tax system is lighter on farm households than on other households for similar levels of income (OECD, 2001).

Social security systems usually aim to extend an adequate level of social protection, in general through pension, health and unemployment schemes, to all members of society. Some countries offer special terms to farmers. This is the case in one third of OECD countries with respect to old age pensions where governments may contribute through an appropriation from general revenue, or pay a subsidy to make up any deficit in the insurance fund. In some countries, regulations allow farmers to contribute less for the same coverage than other citizens.

Social transfers are often the second source of off-farm income for farm households after earnings from non-agricultural activities. In some countries, they are the most important source of non-farm income. In the mid-90s they accounted for around 10% of all farm household income in countries where farm households are broadly defined and from 5 to 25% in countries were farm households are narrowly defined (OECD, 2000).

The impact of social transfers on the disposable income (total income minus taxes) of farm households is significant (OECD, 2001). Low-income rates for farm households of between 20 and 40% before tax and social transfers fall to 10-20%. Social transfers have been effective in reducing the incidence of low income, especially for households with an older head. These households receive the highest benefits from social policies, mainly in the form of pensions. Nonetheless, social transfers have a greater effect on the disposable income of non-farm households than on farm households. In fact, in most countries examined, the share of social transfers in total income is relatively smaller for farm households than for other households (OECD, 2001). This could be explained by the fact that farmers are mostly self-employed. Unemployment benefits are therefore less important. However, with the increase of income from non-agricultural activities in total farm household income, unemployment benefits may begin to contribute more to the alleviation of low income among farm households in the future.

14. As reported in the PSE database. It should, however, be noted that there may be tax exemptions in other countries that are not covered in the database because the information is not available.

Are policy measures effectively achieving the set objectives in terms of the level, variability and distribution of farm household incomes?

Overall, support policies, whatever their objectives, do raise farm income levels to some extent and reduce their variability, but this would seem to be achieved at significantly greater cost to consumers and taxpayers than necessary. The evidence presented here suggests that there are significant problems in delivering income support to farm households through the types of sector specific measures and policies that have been pursued to date. The main problems relate to ***targeting*** – the great bulk of the measures used are generic in nature – to ***equity*** – because the measures are still predominantly based on production or factors of production they fail to change the income distribution in any significant way and most of the support that reaches the sector goes to larger farm households, who do not usually need it – and to ***leakages*** – much of the support is transferred to unintended beneficiaries.

Income risk management programmes have often provided unnecessary and unintended support because of adverse selection, moral hazard[15] and rent seeking from producers whose objective is to maximise their benefits (Skees, 2000). Moreover, most of these risk reducing policy measures do not take account of all sources of income. Such programmes have probably discouraged the development of private mechanisms. In many cases, the continuation of high support level has slowed adjustment to more viable and sustainable types of farming, or to other activities.

In addition, because much of the support in OECD countries is linked to production or input use there has been significant international spillover effects. Production enhancing support raises domestic farm income but contributes to lower world prices, which in turn depress farm income in other parts of the world. Policies that reduce income risk faced by farmers also affect production decisions, often to the same extent as price support. In addition, by reducing adjustment in the domestic market, they transfer domestic instability to the world market and therefore switch the burden of adjustment to other countries (OECD, 2003*a*).

Which policy instruments would transfer income to farm households more effectively and more equitably?

To design and implement efficient policies, income objectives have to be clearly defined in the national policy process. In particular, some income criteria need to be developed to define and identify the targeted households. All sources of income should be taken into account in identifying the households to be targeted, as well as household wealth. For example, criteria could be set concerning the aggregate level of income or the individual level and variability of individual farm household income that would trigger intervention, if indeed the prevailing policy concerns involve those criteria.

There are several possible policy responses to low-income problems among farm households. Government should first consider ways to develop market solutions. It is important to understand the cause of low income in order to find the most effective remedy. If governments are unwilling to see less efficient farmers leave the sector because they provide economic and social benefits that are not, and cannot be, rewarded by the market, the optimal policy would be to give farmers the appropriate

15. Adverse selection and moral hazard occur when information is asymmetric. Moral hazard refers to the fact that farmers, who know more about their own risk than programme managers or subsidised insurance companies, are encouraged to adopt a riskier behaviour to obtain more indemnities. Adverse selection occurs because farmers are better able to judge whether they will benefit from a programme. As a result, the level of risk in the subscribing population is higher than in the total population.

incentive to provide for these benefits, using for example decoupled and targeted payments rather than redistribute support only on the basis of lower incomes.

Similarly, regarding income risk management, government should encourage the development of contingency arrangements such as insurance and futures markets, for example through the collection and transmission of information to reduce problems created by information asymmetry; or training programmes in the use of futures markets to reduce income risk. Agricultural safety nets could then be envisaged to address any remaining risk management failure.

From an income transfer efficiency point of view, support that is decoupled from agricultural activity and targeted specifically to income would be much better as a way to transfer income to farm households. Such direct income payments minimise economic distortions and distributive leakages because their effects on production decisions are minimal, and they can be targeted and delivered to those households that are deemed to warrant assistance.

More generally, government could invest in general services for the sector, such as expenditures on infrastructure, training, research and development, that improve the functioning of agricultural markets and allow farmers to increase their competitiveness. Low income may be experienced by farm households that are resource-poor and located in areas where there is also a problem of lack of viable economic alternatives. The solution in this type of situation is not necessarily a sector-specific income support scheme. Investment in infrastructure to make rural areas more attractive to investors and transitional assistance to more viable economic activities may be of greater benefit.

Sequencing is important. As policies to address market failures in the agricultural sector will have an impact on the income of farmers, there is a logical case for applying measures that first correct market failures and then address any outstanding concerns about incomes, using the types of measures indicated above. Finally, general tax and social security systems are in place in most, if not all, OECD countries. These structures are well placed to identify remaining low-income problems among agricultural households and ensure equal treatment vis-à-vis other classes of households.

It is important, in order to assess the problems and needs of the sector and to implement targeted measures, that comprehensive information on the economic situation of farm households be available. Such information should be collected in a flexible way to allow assessment and monitoring of income deficiencies. More detailed information on the sources of non-farm income would also help to understand the various strategies adopted by farm households and the relationships between agricultural, fiscal and social policies. Available statistics, however, show that in many countries, income support policies have been designed and implemented in the absence of adequate information on the income situation of farm households. This fact must, in part, explain their poor performance.

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OVERVIEW OF THE AGRICULTURAL AND RURAL INCOME SITUATION AND TRENDS IN THE COMPOSITION OF INCOME IN ESTONIA

By Ms. Jaanika Udras and Ms. Marju Aamisepp
(Paper presented by Ms. Katrin Puhm)

Abstract

During the years 1996-2001 the rate of employment in Estonia has been on average 60% of the total working population, whereas the employment rate of the rural population has been 55% of the total working rural population. The number of employees in agriculture has decreased over the years; in 1996 8% of the total working population was employed in agriculture, by 2002 the number had decreased to 5% of the total working population. In this presentation the incomes of Estonians are reviewed. On the basis of the data of the Estonian Statistical Office, the income of the average Estonian household and its structure are described in general. It is followed by a comparison of the structure of incomes of town households and rural households and thereafter the incomes of agricultural producers on the basis of FADN are being analysed. Finally the part of state aid to agriculture is discussed. Because there is no direct statistical account on the incomes of those employed in agriculture from activities other than agriculture, it can be estimated only indirectly. Comparison with the incomes of agricultural producers of other countries has been made on the basis of net factor profit (EAA methodology) and support rate per producer.

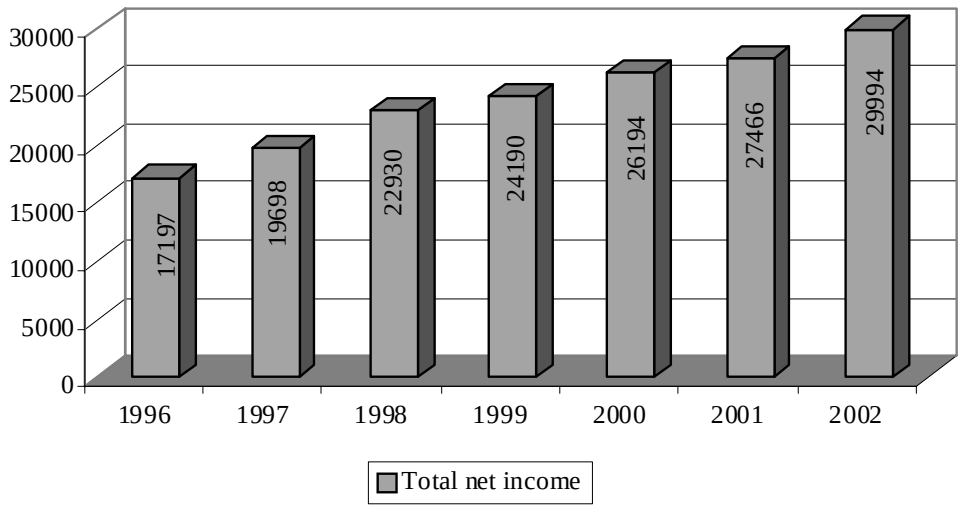
Income structure and income situation in Estonia

The comprehensive state statistics on the income of the population has been published regularly since 1996. The statistical indicators collected during the study of the budget of a household characterise incomes by the following elements:

- Income from wages and salaries.
- Income from individual work:
  - Income from activities related with agriculture and forestry.
  - Income from non-agricultural activities.
- Increments:
  - Pension.
  - Child support.
- Other income.
- Non-monetary income.

According to the official statistics about household income, the number has increased from year to year (Diagram 1). In 1997 and 1998 income increased by 15% on average, compared to the previous years, 5% in 1999 and 2001 and about 10% in 2000 and 2002. Compared with 1996, the average household income in 2002 has increased by 74%.

Diagram 1. Household annual net income (in kroons)



Source: Statistical Office of Estonia.

The largest share of total income comes from salaries and wages, *i.e.* about 60% on average (Table 1). Increments comprise about 20-25%, income from individual work about 5-10%, other income about 2% and property income is less than 1%.

Table 1. Share of different income sources in total annual income of the household (%)

	1996	1997	1998	1999	2000	2001	2002
Income from wages and salaries	62.9	61.3	64.2	61.1	63.2	63.4	64.5
Income from individual work[1]	10.8	10.7	6.0	5.4	5.1	4.9	5.2
Income from activities related with agriculture and forestry	81.6	67.3	67.7	60.9	55.2	59.2	55.2
Income from non-agricultural activities	18.4	32.7	32.3	39.1	44.8	40.8	44.8
Income from real estate	0.4	0.2	0.4	0.6	0.8	0.8	0.5
Increments	23.3	24.8	23.8	27.0	25.6	25.0	25.0
Pension	*72.0*	*73.8*	*72.4*	*74.9*	*70.6*	*71.5*	*71.2*
Child support	13.1	11.9	13.4	12.1	13.1	12.4	11.8
Other income[2]	2.0	1.4	1.6	1.6	1.7	1.7	1.4
Non-monetary income	0.6	1.6	3.9	4.3	3.7	4.2	3.5

1. The profit from individual professional work also contains the self-produced food products converted to monetary value.
2. Other incomes include property income and other income.

Source: Statistical Office of Estonia.

The non-monetary part of income has been growing steadily from 0.6% in 1996 to 3.5% in 2002. About half of the income from individual work comes from agricultural and forest activities, 70% of the increments are pension, and about 10% is child support.

Comparison of the structure of the incomes of a member of rural and town household

While looking at Tables 2 and 3 it can bee seen that the number of town households during the years 1996-2002 has been on average 63% larger than the number of rural households. The town households have had around 20% higher net income during the observed years, whereas the income from paid employment has been more than 35% higher than for the members of rural households. The town household has also received more transitions (around 10%), also pensions, sickness benefits, alimonies and supports, other transitions and profits and also non-monetary profits. At the same time the average size of rural households has been 10% larger than town households, and there are 32% more children in rural households than in town households.

Table 2. Average net income of a town household per month (in kroons), 1996-2002

	1996	1997	1998	1999	2000	2001	2002
Number of households	447 610	458 256	463 847	427 661	410 220	404 538	402 528
Average size of a household	2.3	2.3	2.2	2.2	2.3	2.3	2.3
Average number of children	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Net income	**1 501.1**	**1 747.3**	**2 043.5**	**2 162.5**	**2 326.2**	**2 430.2**	**2 667.7**
Income from paid employment	996.8	1 124	1 377.4	1 386.6	1 527.7	1 604.6	1 795.8
Profit from individual professional activities	120.1	153.5	80.7	81	84.5	80.3	94.5
Transitions	338.9	414.5	462.6	555.8	571.6	575.2	627.2
Pensions	243.5	308.3	338.4	419	407.1	413.2	445.5
Unemployment benefit	1.8	2.5	2	4.1	5.8	6.6	4.4
Child benefit	40.9	43	53.8	58.3	66.8	63	66.9
Sickness benefit	5.5	3.4	4.6	14	14.6	12.4	19.5
Alimonies and supports	15.6	14.2	15.3	18.4	15.2	10.7	13.3
Social assistance	14.1	13.4	9.4	12.6	12.1	20.3	26.5
Other transitions	17.5	29.7	39.1	29.4	50	49	51.1
Other profits	37.1	28	42.3	48.1	57.1	55.8	48.6
Non-monetary profits	8.3	27.4	80.5	91	85.3	114.3	101.6

Source: Statistical Office of Estonia.

From Table 3 it can also be seen that the rural population has earned income from other professional activities (the latter includes income from sales of horticultural products; sales of livestock and poultry and fishery products; sales of apiculture; sales of timber, other incomes such as sales of firewood, berries and mushrooms etc.), which includes both agricultural and non-agricultural activities, more than 50% more than town households. The unemployment rate is higher in rural areas, therefore 7% more unemployment benefits have been paid to the rural population than to the town people. Also, the rural population has received more child benefits and social assistance due to larger households.

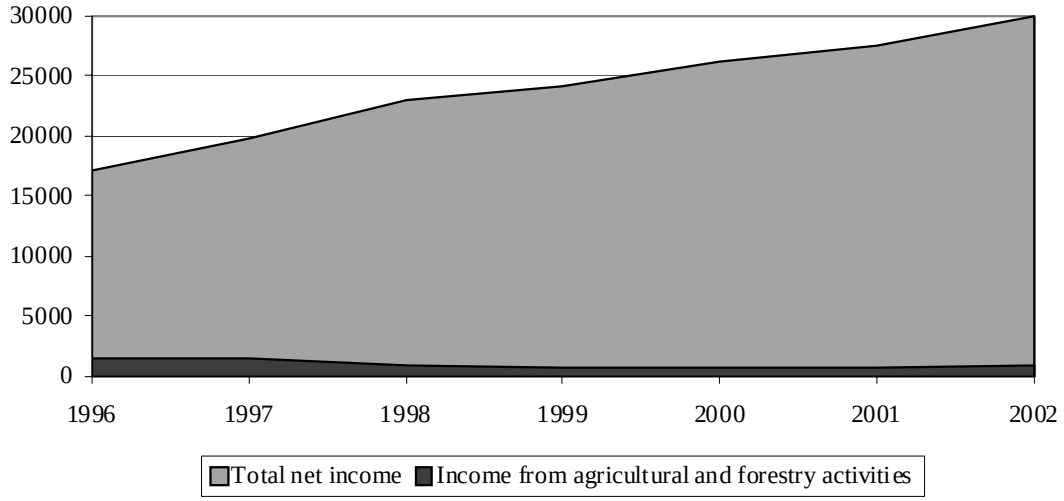
Table 3. Average net income of a rural household per month (in kroons), 1996-2002

	1996	1997	1998	1999	2000	2001	2002
Number of households	144 661	145 671	150 473	166 473	165 076	164 682	164 141
Average size of a household	2.5	2.5	2.5	2.5	2.6	2.5	2.5
Average number of children	0.7	0.7	0.6	0.6	0.6	0.6	0.5
Net income	**1 237.4**	**1 339**	**1 550.9**	**1 673.5**	**1 866.4**	**1 9728**	**2 119.4**
Income from paid employment	629	669.3	818.6	870.4	1 053.5	1 110.7	1 197.4
Profit from individual professional activities	255	240.2	208.8	174.6	166.1	179.8	207.2
Transitions	320.6	385.9	434.4	519.4	527.2	567	616.7
Pensions	232.5	278.4	305.8	383	363.8	401.6	441.4
Unemployment benefit	2.5	2.5	2.8	4.2	6.2	5.2	4.9
Child benefit	52.4	64.7	79.7	82.9	86.6	88.3	88.4
Sickness benefit	2.9	3.2	4.4	4.7	23.8	12.1	10.7
Alimonies and supports	5.7	11.1	5.1	9.8	10.5	5.8	6
Social assistance	15.9	19	22	22	21.9	32.4	43.8
Other transitions	8.7	7	14.6	12.8	14.4	21.6	21.5
Other profits	26.1	23	27.6	35.7	49.8	56.7	43.4
Non-monetary profits	6.7	20.5	61.5	73.6	69.8	58.6	54.7

Source: Statistical Office of Estonia.

Diagram 2 compares the average income of a household with the income from agriculture and forestry sector. The household net income has increased from year to year, whereas the income from agriculture and forestry activities has decreased. In 1996 agricultural activities comprised about 9% of net income. In 1996 total income of Estonians was 11 times higher than the incomes from agriculture and forestry activities. By 2002 this gap had increased 3 times, *i.e.* total income is 35 times higher than income from agriculture and forestry activities.

Diagram 2. The Estonian average net income of a household as compared to the income from agriculture and forestry activities



Source: Statistical Office of Estonia.

The income by counties describe the relative economic environment (Table 4) there. During the observed years, the income in Tartu, Harju and Ida-Viru counties from agriculture and forestry activities have remained below the average Estonian income. During some years, the income in Valga county also remained below the average. It could be said that the income of these counties does not depend on agricultural activities, since the first three counties are Estonian counties with the largest towns and where the major part of the population work in towns. Järva, Saare, Hiiu and Lääne counties depended more on agricultural incomes during the years 1996-2002. It can be said that in these counties people are active in agriculture in addition to other activities and that income from agriculture is relatively important.

Table 4. Income from agriculture and forestry activities by counties per household member (in kroons)

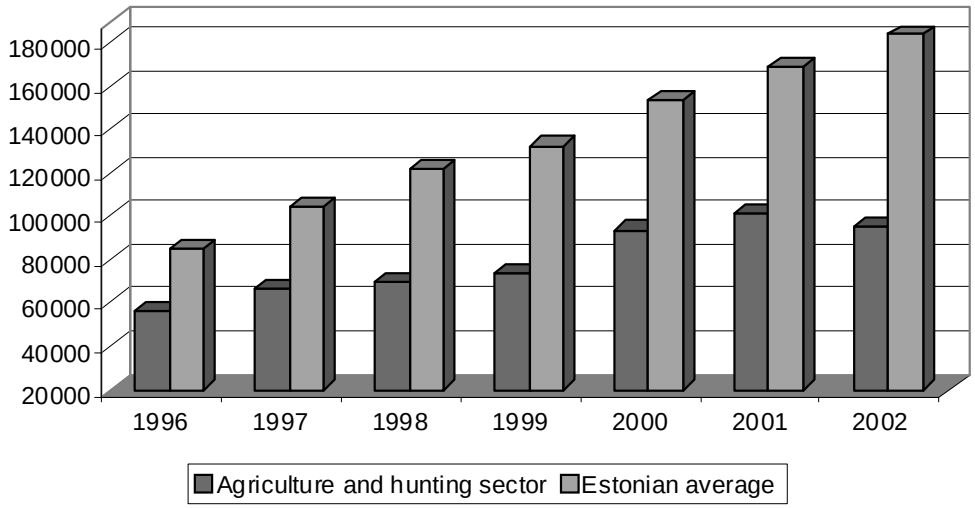
	1996	1997	1998	1999	2000	2001	2002
Lääne-Viru	2 562	1 609	1 490	1 157	914	1 198	2 426
Lääne	1 808	1 931	1 890	1 136	1 442	1 120	2 314
Hiiu	2 114	2 464	1 398	1 919	1 373	1 673	2 200
Viljandi	2 770	1 938	1 526	1 538	965	1 645	2 200
Rapla	2 311	2 503	1 592	1 049	1 741	1 612	1 733
Saare	3 523	2 996	1 330	1 487	1 228	2 138	1 714
Jõgeva	2 548	2 315	1 548	1 290	1 765	888	1 175
Põlva	1 925	1 466	1 414	1 504	648	1 277	1 171
Järva	1 978	2 472	2 124	1 850	1 181	1 218	1 086
Võru	2 148	3 862	1 432	1 282	1 135	1 225	989
Valga	3 074	1 642	1 459	228	382	575	941
Pärnu	2 248	1 975	2 084	984	875	905	798
Tartu	1 446	1 300	822	640	846	937	636
Harju	850	883	377	372	403	379	444
Ida-Viru	884	864	582	926	577	600	367
Estonian average	**1 517**	**1 421**	**936**	**797**	**730**	**792**	**856**

Source: Statistical Office of Estonia.

Rate of return and salary in agriculture

The percentage of agriculture in gross domestic product (GDP) decreased constantly since the end of the 1980s and comprised 3% in 2002. GDP per employee has increased in the agriculture and hunting sector since 1996 (Diagram 3). If, in 1996 the GDP in the agriculture and hunting sector was 56 136 kroons per employee, then by the year 2001 this sum had risen up to 100 982 kroons per employee, so the average income in agriculture and hunting increased almost 80% in six years. However, in 2002 GDP per employee in the agriculture and hunting sector decreased more than 5% as compared to 2001. The cause for the decrease of GDP was the decrease in production due to a long drought and the decrease in Estonian prices because of the fall in prices of milk and pork meat on the world market. During the observed years GDP per employee in the agriculture and hunting sector has been on average 40% lower than the GDP per average Estonian employee. Therefore the income of the people employed in agriculture has, during the years of 1996-2002, been lower than the income of an average Estonian by more than a third.

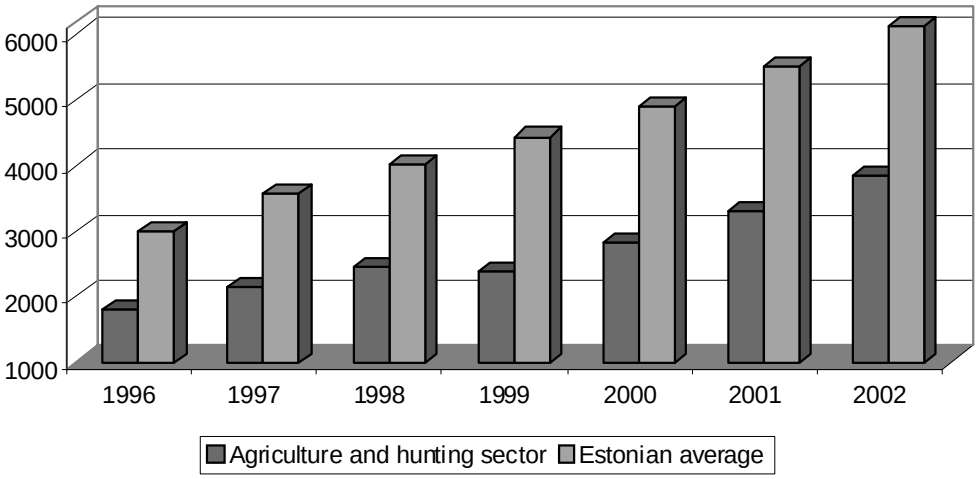
Diagram 3. GDP per employee



Source: Statistical Office of Estonia.

The payment for the additional value created in agriculture is shown in Diagram 4. At the lowest level the average salary paid in agriculture and hunting in 1999 was 53.7% of the country average, that is, the year after the Russian crisis. During the following years the ratio improved moderately and reached 62.9% in 2002.

Diagram 4. The Estonian average net income of a household member per year as compared to the income from agriculture and forestry activities

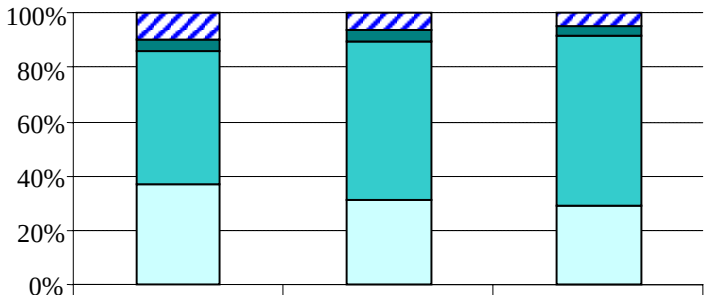


Source: Statistical Office of Estonia.

Analysis of the income of agricultural producers on the basis of FADN data

The income of an agricultural enterprise consists of the value of the crop and animal husbandry production, also the value of the rest of production, and in addition of the supports directly connected to the production. For the purpose of analysis agricultural producers were grouped according to economic size and production type and the structure of their incomes during the years 1999-2001 was observed. Structure of incomes by years has been very different (Diagram 5).

Diagram 5. Income structure, 1999-2001



	1999	2000	2001
Supports	9.6%	6.1%	5.1%
Other production	4.5%	4.1%	3.5%
Livestock production	49.0%	58.2%	62.3%
Crop production	36.9%	31.7%	29.1%

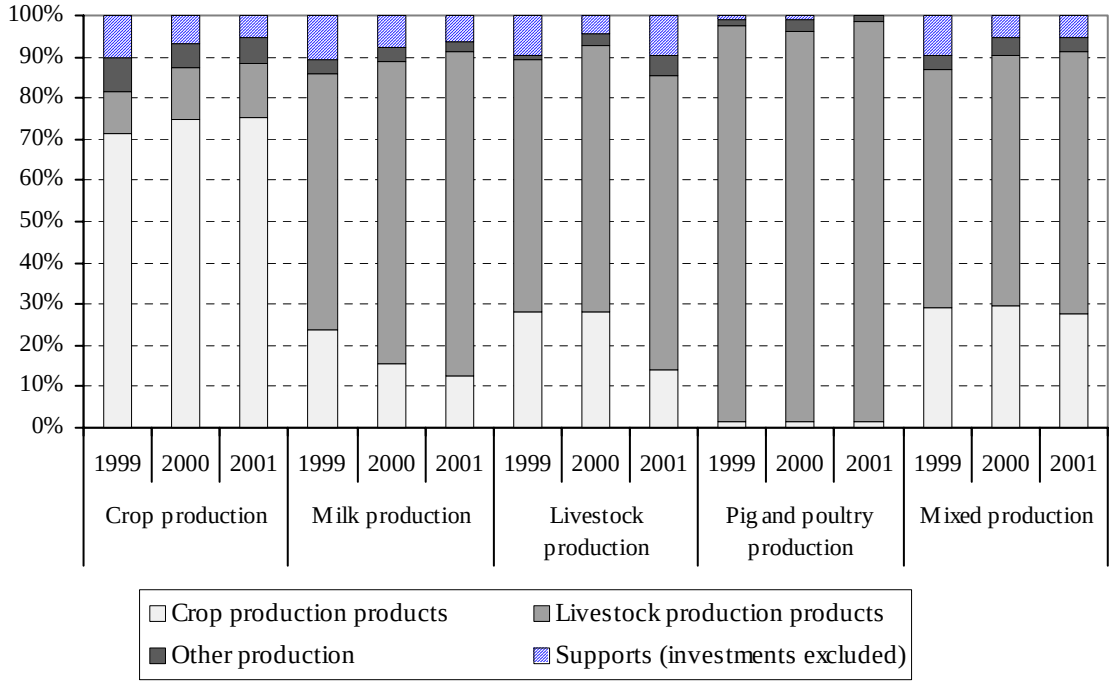
Source: Jäneda Training and Advisory Centre.

During the years 1999-2001 only the percentage of livestock production in the structure of incomes has increased. The percentage of livestock production in incomes has increased up to 62% by the year 2002, however the percentage of crop production and other production[1] has decreased. The percentage of support in incomes has also decreased – in 1999 support made up 9.6% of income, but in 2001 the level was only 5.1%.

By the production branches the tendency is the same – the percentage of livestock production has increased and the percentage of crop and other production has decreased (Diagram 6). An exception here is crop production, where the percentage of crop produce has increased, and livestock production, where the percentage of support and other production increased.

1. Other production includes other cultivation practices of field and horticulture except crop and livestock production, *e.g.* sales of timber and forest, services provided for others and rent fees.

Diagram 6. Income structure by production branches, 1999-2001



Source: Jäneda Training and Advisory Centre.

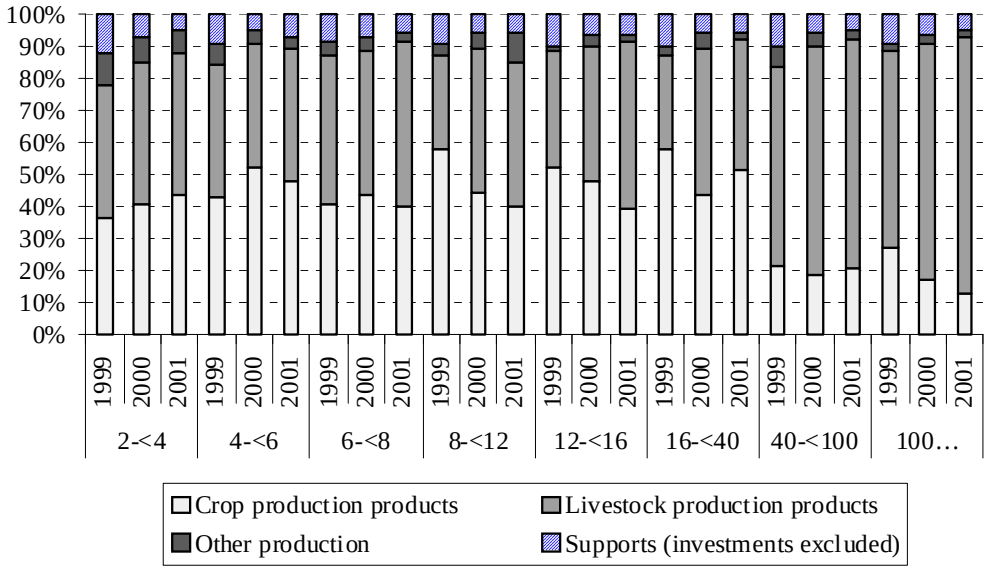
The largest specialisation can be seen in pig and poultry farming, which involves very little crop and other production. Representatives in this production type have also received the least support, below 1%. In 1999, most support was received by entrepreneurs involved in milk production – 10.7%, and they were followed by people involved in crop production (10.3%). Livestock and mixed type producers received 9.6% of support. However, in 2001 support made up the most important part in the livestock production type enterprises (9.9%).

The percentage for milk producers was on average 6.5%, mixed type producers 5.5% and crop producers 5.2%. Support was almost non-existent in pig and poultry farming production (0.2%).

The analysis of incomes by economic size of agricultural enterprises is shown in Diagram 7. While in smaller companies income from crop and livestock production has been distributed more or less proportionally, in the bigger economic holdings (more than 40 ESU[2]) livestock production is clearly dominant. Consequently, among the smaller enterprises, mixed production is dominant, and in the larger ones, specialising has been towards livestock production. In the larger enterprise group, ancillary activity makes up a smaller part of income than in the case of small producers. This, too, indicates specialisation towards a specific branch of production. The proportion of support in income is highest in the enterprises of average size.

2. In the European Union the European unit *(**ESU**-European Size Unit),* which is equal to EUR 1 200 is used to determine **the economic size of an enterprise**. On dividing the standard total revenue of an enterprise with EUR 1 200, the economic size of an enterprise in ESUs is received.

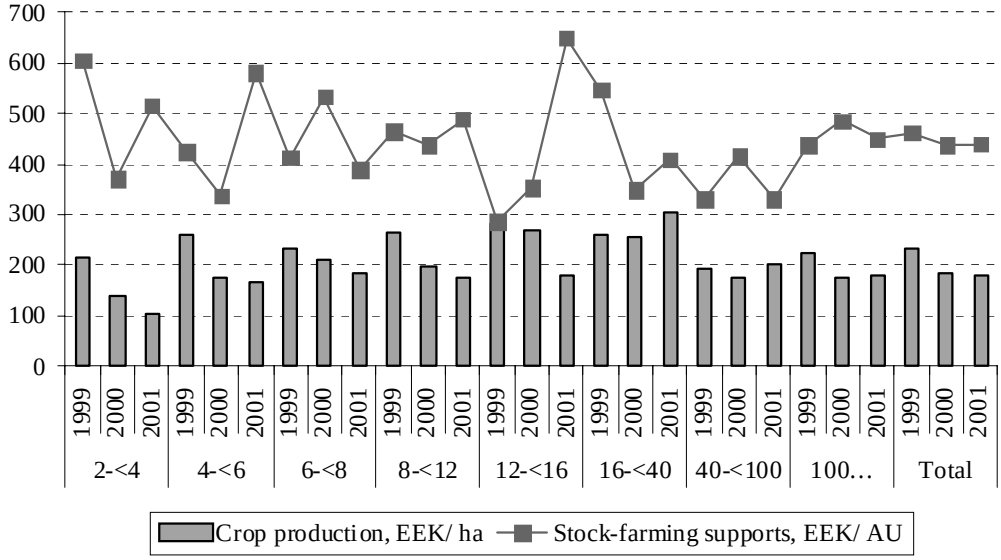
Diagram 7. Income structure by the economic size of the agricultural enterprise, 1999-2001



Source: Jäneda Training and Advisory Centre.

The volume of crop production support per agricultural land has decreased from 234 kroons to 180 kroons per hectare, as an average of all enterprises (Diagram 8). While in 1999 most support was received by companies with an average economic size of 12 to 16 ESU, in 2001 most support was received by larger companies with an economic size of 16 to 100 ESU.

Diagram 8. The volume of support by units, 1999-2001 (in kroons)



Source: Jäneda Training and Advisory Centre.

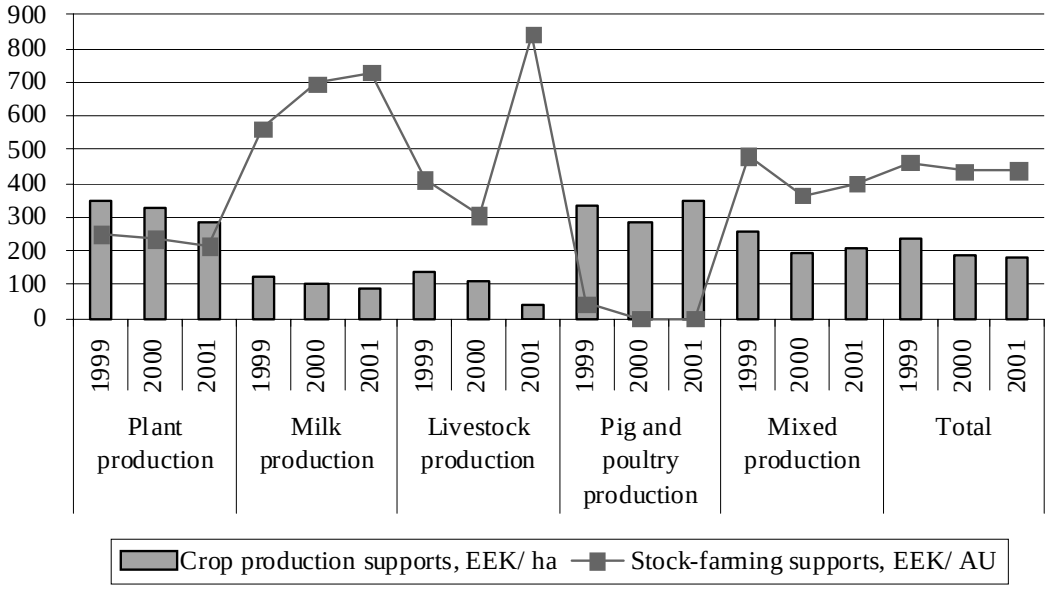
The support to stock-farming has remained on the level at a little over 400 kroons per livestock unit. In 1999 as well as in 2001 smaller producers with an economic size of 12 to 16 ESU have received more support than others and most support has been received by the ones in the group of 12 to 16 ESU; 649 kroons per livestock unit.

The volume of support by production types can be seen in Diagram 9. During the years 1999-2001 most crop production oriented support was received by companies of crop production, pig and poultry farming, approximately 300 kroons per hectare. The sum of support was nearly 3 times smaller for companies dealing with milk and livestock production. Most crop production oriented support has been granted to companies of pig and poultry production, on average 429 kroons per hectare during the three observed years, with the least by livestock production companies, on average 97 kroons per hectare.

The most support per livestock unit has been granted to companies that produce milk, 663 kroons on average during the three years, followed by companies involved in livestock production who received an average of 519 kroons of support per livestock unit. However, in pig and poultry farming this kind of support practically did not occur and only in 1999, companies of this type of production received support of 44 kroons per livestock unit.

The data shown in diagrams 8 and 9 directly relates to the structure of agricultural producers.

Diagram 9. The volume of support by production type, 1999-2001



Source: Jäneda Training and Advisory Centre.

State aid to the agricultural sector

The agricultural policy implemented in Estonia during the 1990s is characterised by low state interference and pressure arising from the general liberal trade regime on domestic prices. After laying down the legal bases for the organisation of agricultural markets in 1995, the calculation of the need for support on the basis of the estimated income deficit and the annual negotiations of the Government of the Republic of Estonia and the representatives of agricultural producers was started. This calculation reflected the financial-economic prognosis on the production volumes of the next year, on which the production value on the basis of the predicted domestic market prices and applied for prices which ensure economic profitability, was calculated. The basis for the calculation of target prices is the actual expenses related to production and the investment expenses made to bring into accordance with requirements. It was also presumed that a person employed in agriculture would receive the same reward as persons in other sectors of the economy. The estimated income deficit is the basis for the bilateral agreement on the need for support paid to the agricultural producers.

The calculated income deficit during the last years has been estimated at 800-1 000 million kroons (Table 5). With the help of support paid in Estonia so far approximately 50% can be covered, *i.e.* 400-500 million will remain in deficit.

Table 5. State aid to agriculture in million kroons

	1996	1997	1998	1999	2000	2001	2002
Calculated income deficit	605.5	1 297.5	1 511.7	1 271.5	2 518.0[1]	1 147.3	801
Income supports			188.1	239.2	239.8	227.0	227.7
Development supports	83.3	119.6	207.0	203.7	75.8	70.6[2]	235.4[3]
Partial compensation of damages by the weather			227.0				101.0
Other supports	80.3	54.5	52.8	54.9	74.5	101.6	116.2
Total	163.6	174.1	674.9	497.9	390.1	399.2	680.3
Supports to GDP, %	0.35	0.31	1.02	0.72	0.50	0.46	0.72
Supports to GDP of agriculture, %	6.01	6.26	24.02	19.27	14.54	13.92	24.29

1. The sum of 2002 includes the investment deficit of previous years.
2. Includes the EU support in the sum of 4.6 million.
3. Includes the EU support in the sum of 126.5 million.

Source: Ministry of Agriculture.

The total sum of agricultural support has increased year-by-year. In 1996 agricultural producers were paid 163.6 million kroons in support, then in 2002 farmers received 680.3 million kroons. The support paid to producers has grown more than four times in seven years. During the observed period agricultural producers have been paid crop failure support in two years, *i.e.* partial compensation of damages caused by a natural disaster, in 1998 for excessive moisture and in 2002 for drought. In 2001 Estonian agricultural producers started to receive money within the European Union SAPARD programme. Due to that, the sum of development support in 2002 increased by 233% compared to 2001. The relationship of support to total Estonian GDP has grown two times as compared to 1996, *i.e.* from 0.35% to 0.72%. Therefore we can say that the value created in Estonia below 1% has been directed for the support of agriculture over the year. The relationship of support to GDP has grown seven times in seven years, *i.e.* in 1996 support granted by the state constituted only 6.01% of the value created in agriculture However in 2002 it was already 24.29% or one fourth of the value created in agriculture was agricultural support. Also, as can be seen from Table 5, the relationship of support to Estonian GDP and agricultural GDP was significantly higher in 1998 and 2002 than during other years. The reason for that is compensation by the state for the difficult economic situation in agriculture.

Comparison of the incomes and supports of the agricultural producers

Comparing the relationship of all Estonian support to GDP with the same indicator of other countries (Table 6), it can be seen that the same indicator of Estonia is on average only a little lower than in other countries or in EU and OECD member states. However, it is remarkable that the index of the rate of return to producers, which indicates the total sum of the difference between national support paid to agricultural producers, and the consumer's and producer's price, is several times lower in Estonia than in other countries. Although support has been received on relatively the same level to GDP, the difference between the producer and consumer price is significantly smaller.

Table 6. Indexes of agricultural support by countries, 1996-2000 (%)

		1996	1997	1998	1999	2000[1]	2001[2]
Estonia	Percentage of supports in GDP	1.2	0.9	2.2	0.7	0.7	1.0
	PSE, %	7	6	20	6	7	13
Latvia	Percentage of supports in GDP	0.7	0.7	2.3	2.1	1.5	1.5
	PSE, %	3	5	20	22	15	16
Lithuania	Percentage of supports in GDP	0.8	1.4	2.8	2.6	1.2	1.5
	PSE, %	1	4	16	16	6	11
European Union	Percentage of supports in GDP	1.6	1.6	1.6	1.6	1.4	1.4
	PSE, %	32	32	36	39	34	35
OECD	Percentage of supports in GDP	1.5	1.4	1.5	1.4	1.3	1.3
	PSE, %	29	28	33	35	32	31

1. Provisional.
2. Estimate.

Source: OECD, PSE/CSE database.

The year 2002 was economically more difficult for agricultural producers than the year 2001. The indicators of both production and income decreased in 2002 as compared to the previous year, at the same time production expenses increased. The income of the entrepreneurs active in agriculture decreased in Estonia in 2002 as compared to 2001 by 10.3%.

Agricultural income per employee in Estonia was more than six times smaller than the average in EU member states in 2001 and 2002. However, it was approximately 1.5 times higher than in Latvia (Table 7). So, Estonian farmers received almost 80% lower incomes than the average EU farmer. If you look separately at the neighbouring country of Estonia – Finland, agricultural producers in Finland received more than 80% higher incomes from agriculture than Estonian agricultural producers. Estonian farmers receive supports from GDP at approximately the same level as Latvia, Lithuania, EU and OECD countries (see Table 6), but the producer's income received from the producer and consumer price is minimal in Estonia. Because of the economic factors and Estonian policy, agricultural producers in Estonia receive incomes that are several times lower than in countries of the EU and OECD. Therefore, we believe that there will be a large gap and a lot of tension between the different sectors on the high incomes of farmers after the accession and the implementation of the measures of the Common Agricultural Policy. During the first stage, the work of those employed in agriculture should be rewarded equally.

Table 7. Factor income[1] per labour unit in thousand euros

	2001	2002
Estonia	2.5	2.4
Latvia	1.4	1.5
Finland	13.2	14.0
EU 15	16.1	15.7

1. The real income of factors in agriculture, per annual work unit, corresponds to the real net value added at factor cost of agriculture, per total annual work unit. Net value added at factor cost is calculated by subtracting from the value of agricultural output at basic prices the value of intermediate consumption, the consumption of fixed capital and production taxes, and adding the value of production subsidies.

Source: Ministry of Agriculture.

Summary

The average salary of salaried work has increased in the agriculture and hunting sector over the past years, but still comprises only a little over 60% of the average gross salary of the country. In the income of rural households, the share of income from agricultural and forestry activities has decreased. The income of agricultural producers from crop production, other production and support has decreased during 1999-2001, while the income from livestock production has increased.

State aid to the agricultural sector has during the past years been below the level of 1%, reaching it only with the help of support paid in compensation for the extraordinary weather conditions. Besides, sales of the final product on the domestic market was suppressed due to the liberal trade regime and low prices, while all the inputs necessary for agricultural production have been available for years at relatively high world market prices. In this situation the sector has experienced a lack of investment for years, although it has been alleviated during the past year by the payment of support from the SAPARD programme. However, due to the above, the productivity level in agriculture is relatively low and therefore the level of income is low for producers and thus concurs the continuous tightening of the sector.

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TRENDS IN AGRICULTURAL AND RURAL INCOMES IN LATVIA

By Ms. Valda Bratka, Ms. Ginta Uzulina, Ms. Aija Vucane and Mr. Ritvars Zapereckis
(Paper presented by Ms. G. Uzulina)

Abstract

This report discusses the trends and structure of agricultural and rural incomes in Latvia, using several sources of statistical data. The main objective of this report is to describe the tendencies in the development of living standards of households, which are involved in agricultural production or just live in rural areas. The second objective of this report is to explain policy targets related to increases in income, and to show the relation between income level and policy instruments. In the report, statistical data from Household Budget Surveys, the Farm Accountancy Data Network, the Economical Accounts for Agriculture, as well as data on the average monthly wages and salaries by different activities are used to estimate agricultural and rural incomes, comparing all sources of data.

Trends in agricultural and rural incomes

Sources of data used

There are several sources of data to evaluate agricultural and rural incomes in Latvia. The first source of data is the Household Budget Survey, which was conducted each year since 1995 until 2000. It was organised again in 2002, and now the Central Statistical Bureau is processing and summarising data, which will be officially available in June 2003. The results of the Household Budget Survey give information about total income, expenditures and consumption levels and structures of both households and the main socio-economic groups. This Survey is a source of information on qualitative indicators of the standard of living in different types of settlements and different regions.

The next source of data is the Farm Accountancy Data Network, which is done each year in Latvia since 1997. These data show tendencies in the development of income depending on the economical size of farms and the type of activity. In Latvia, such data are available until 2001, but some of them are not comparable due to the changes and improvements in methodology according to the requirements of the European Union. For example, the regional breakdown of results in 1998 and the breakdown by size of farm in 1999 was summarised differently than in 2001.

The third source of data is information about average monthly wages and salaries in the different sectors of the economy, which shows differences in income between these sectors. These data are useful in analysing the tendencies in labour markets and they also describe the relation between labour supply and demand and also the price of labour in the different sectors of the economy.

And the final source of data for analysis of income is the Economic Accounts for Agriculture, which also characterise the trends in agricultural income.

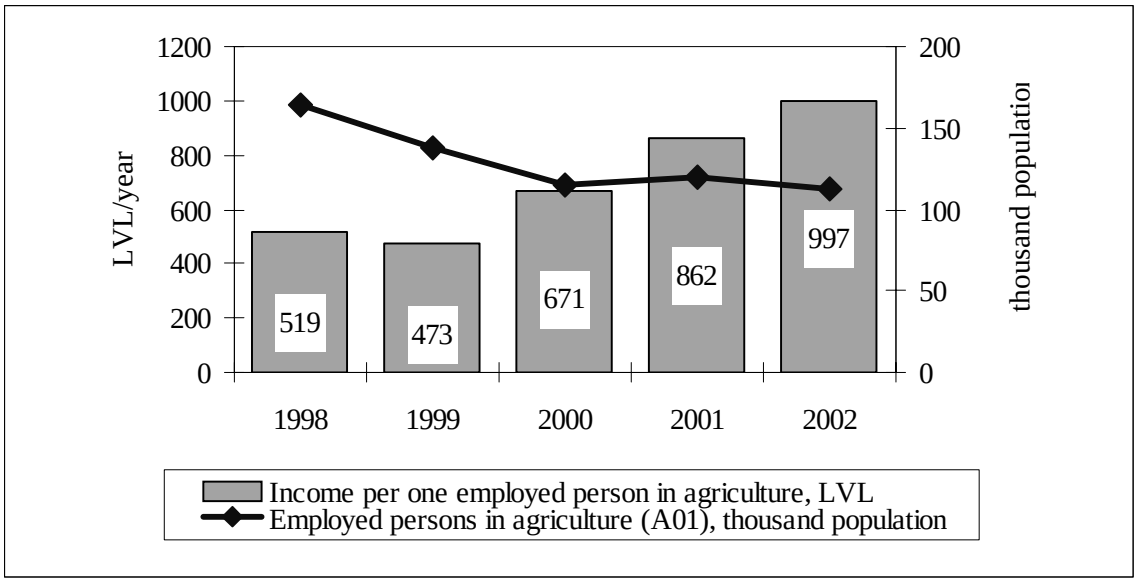
Using all these sources of data, the report explains trends in agricultural and rural incomes in Latvia. Some of the data is available until 2001 or for other time periods, but all of them show the main features of the situation in agricultural and rural incomes.

Level of agricultural income

Analysing the average monthly wages and salaries by kind of activity, the average monthly salary of employees in agriculture was about 60% of the average monthly wages and salaries in the whole economy in 2002. If one compares the share of average monthly wages and salaries in agriculture, hunting and forestry with the average in the economy, then this share is larger at about 77%. In recent years and especially since 2001, the proportion of the average monthly wages and salaries in agriculture has been increasing.

According to the data from the Economic Accounts for Agriculture, the average income per employed person in agriculture has also been increasing annually since 2000, which also proves that the income level in agriculture is improving year by year. It is also linked with the number of employed persons in agriculture, which is decreasing; and hence this could be one of the reasons for the increase in the level of agricultural income.

Figure 1. Income per employed person in agriculture and number of employed persons in agriculture in 1998 –2002, (LVL/year and thousand populations)



Source: The Labour Force Survey and the Economic Accounts for Agriculture.

Structure of farm income

To analyse the structure of farm income based on farm size and also regions, it is useful to estimate the operating results of agricultural producers, which is collected according to principles of the Farm Accountancy Data Network in Latvia.

Analysing operating results of Latvian agricultural producers; the following observations imply that state support comprises a similar share in the total revenue of the different size of farms. It characterises that the relevant part of state support is linked to production units and any increase of agricultural area or in animal numbers give rise to an increase in support. A large share of state support consists of reimbursement of excise tax, which is in between 26% to 37% of total state support depending on size of farm. It shows that this type of state support is very useful for different size of farms.

Table 1. Structure of revenue* by economic size of farm in 2001, %

	Average farm.	1 – 4 ESU[1]	4 – 8 ESU	8 – 16 ESU	16 – 40 ESU	40 - 100 ESU	100 – 250 ESU	250 – and more ESU
Production subsidies, state support	7	5	9	9	10	12	10	4
Of which: reimbursement of excise tax	33	37	26	36	30	37	31	27
Crop production	44	49	45	45	48	56	45	22
Animal breeding	39	44	39	27	21	25	32	53
Other production	10	3	8	19	21	6	13	21
Total	100	100	100	100	100	100	100	100

1. The economic size of farms is expressed into economic size units (ESU). One ESU is a definite EUR value, which as a result of inflation changes over the year. At present 1 ESU=1 200 EUR.

Source: Operating results of Latvian agricultural producers 2001 (Farm Accountancy Data Network).
* Revenue = Output and subsidies, where Output = sales + stock changes + farm use + household consumption.
Sample of survey in 2001 –365 farms.

Comparing revenue levels of farms in different regions, the operating results of agricultural producers show that the largest share of revenue is income from crop production in the Riga and Zemgale regions. It shows the typical farm activities in these regions. Comparing the income of other production, the largest share is in the Kurzeme region – about 13% of total revenue, which means that in this region farms deal with other activities; namely processing, tourism, and other activities.

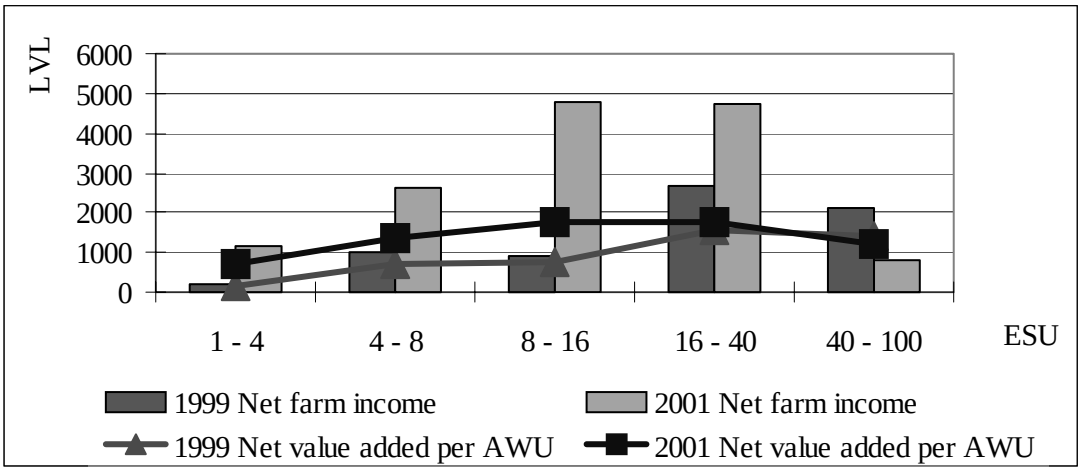
Table 2. Structure of revenue* by regions in 2001, %

	Riga region	Vidzeme region	Latgale region	Kurzeme region	Zemgale region
Production subsidies, state support	4	8	6	6	7
Of which: reimbursement of excise tax	22	37	32	33	31
Crop production	78	45	47	36	53
Animal breeding	16	40	39	44	31
Other production	2	7	8	13	8
Total	100	100	100	100	100

Source: Operating results of Latvian agricultural producers 2001 (Farm Accountancy Data Network).
* Revenue = Output and subsidies, where Output = sales + stock changes + farm use + household consumption.

Describing the net farm income of farms, there is a tendency to get higher net farm income in farms with 8-40 ESU. It shows that productivity is higher in larger farms. Another significant indicator of production is net added value per annual work unit (AWU), which shows the added value of farms using available production sources. This value is related to AWU in order to compare this added value between different farm sizes. Analysing net added value per AWU, the inconsiderable net added value is in small size farms, in the group of farms from 1 to 4 ESU, which again shows that production effectiveness start to increase at a certain production level (Figure 2.).

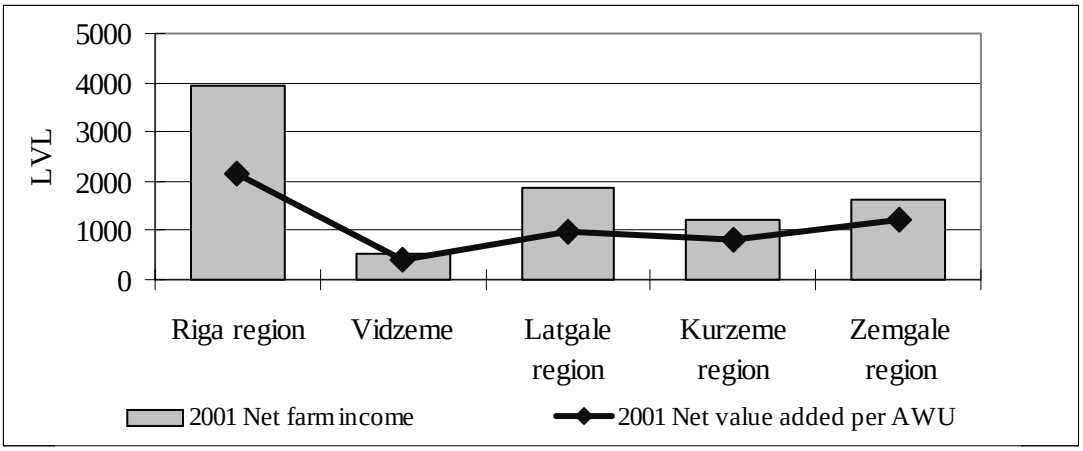
Figure 2. Net farm income and net value added per annual work unit (AWU) by size of farms in 1999 and 2001, LVL



Source: Operating results of Latvian agricultural producers 1999 and 2001 (Farm Accountancy Data Network).

Comparing regional situations, the highest net value added and net farm income is in the Riga region, which could be explained also by the close market possibilities and the presence of good land in this region. In the Latgale region these indicators are also higher than in other regions.

Figure 3. Net farm income and net value added per annual work unit (AWU) in different regions of Latvia in 2001, LVL



Source: Operating results of Latvian agricultural producers 2001 (Farm Accountancy Data Network).

Structure of household income

In the last years the average disposable income of households increased in all households and reached 69.19 lats per household member per month in 2000. The highest increase in disposable income was in urban areas. Household budgets both in urban and rural areas are still based on two main sources of income: compensation for labour and social transfers. The changes in the composition and structure of households' disposable income during the period 1998-2000 are given in Table 3.

Table 3. Structure of disposable income of household (in cash and in kind) in 1998-2000, %

	All household			Urban household			Rural household		
	1998	1999	2000	1998	1999	2000	1998	1999	2000
Disposable income	100	100	100	100	100	100	100	100	100
Of which:									
Compensation for labour	55.8	56.2	57.9	61.9	60.5	61.9	37.8	43.1	44.4
Income from social transfers	26.5	30.0	28.1	24.6	27.7	25.9	32.2	37.1	35.3
Of which: pensions	21.8	24.7	23.6	20.2	22.7	21.8	26.7	30.8	29.7
Net income from agricultural production[1]	6.7	4.2	3.6	1.8	1.5	1.1	21.1	12.4	11.7
Net income from entrepreneurial activity and handicraft	2.8	1.9	1.5	3.4	2.3	1.8	1.0	0.4	0.6
Other income	8.2	7.7	8.9	8.3	8.0	9.3	7.9	7.0	8.0

1. Net income from agriculture production – difference between income (in cash and in kind) obtained after the sale of products manufactured at one's own farm, utilisation consumption requirements and expenditure (in cash and in kind), which are used for the purpose of production, tax payments and other obligatory payments.

Source: The Household Budget Surveys.

According to the Household Budget Survey data, the highest income level was in households in the Riga region. In other regions household income was lower than average income in the country. In the Latgale region, the disposable income was about 71% of average income in the country in 2000.

Table 4. Disposable income of household in 2000

	Riga region	Zemgale region	Vidzeme region	Kurzeme region	Latgale region
Disposable income per one household member per month, LVL	82.76	62.78	62.29	59.85	48.94
Share of average income in the country, %	119.6	90.7	90.0	86.5	70.7

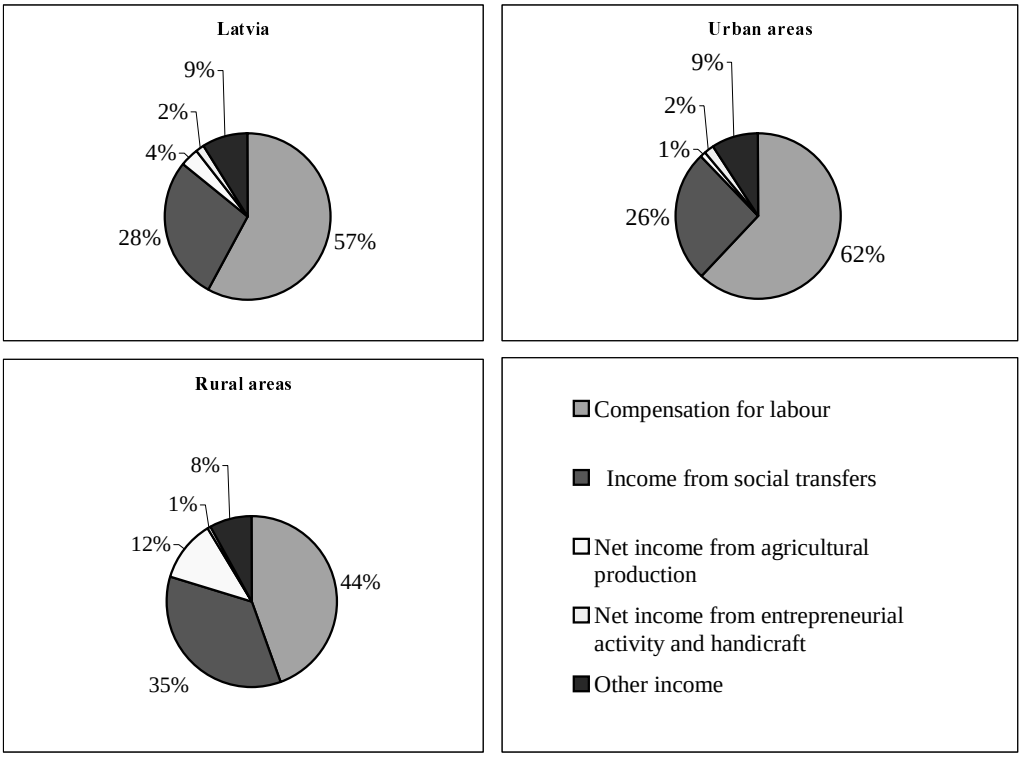
Source: The Household Budget Survey 2000.

The uneven distribution of income has increased in society, for example the Gini coefficient[1] has increased in Latvia from 0.32 in 1998 to 0.34 in 2000, as well as in urban areas it decreased from 0.32 in 1998 to 0.33 in 2000, and in rural areas – from 0.30 in 1998 to 0.33 in 2000.

In 2000, over half of all disposable household income came from compensation from labour, one third (28%) – from social transfers and only 4% was the net income from agricultural production. In rural areas, about 12% of all disposable household income comes from net income of agricultural production as shown in Figure 4. Meanwhile, net income from agricultural production continued to decrease.

1. Gini coefficient indicates how equal the distribution of the total incomes is in the country. It varies from 0 to 1. It is equal to 0, if the equality in income distribution is absolute, and 1 is the opposite. It is calculated according to the consumption expenditures per one consumption unit. The data of the Household Budget Survey have been used in the calculation.

Figure 4. Structure of the disposable household income in urban and rural areas in Latvia, in 2000, %

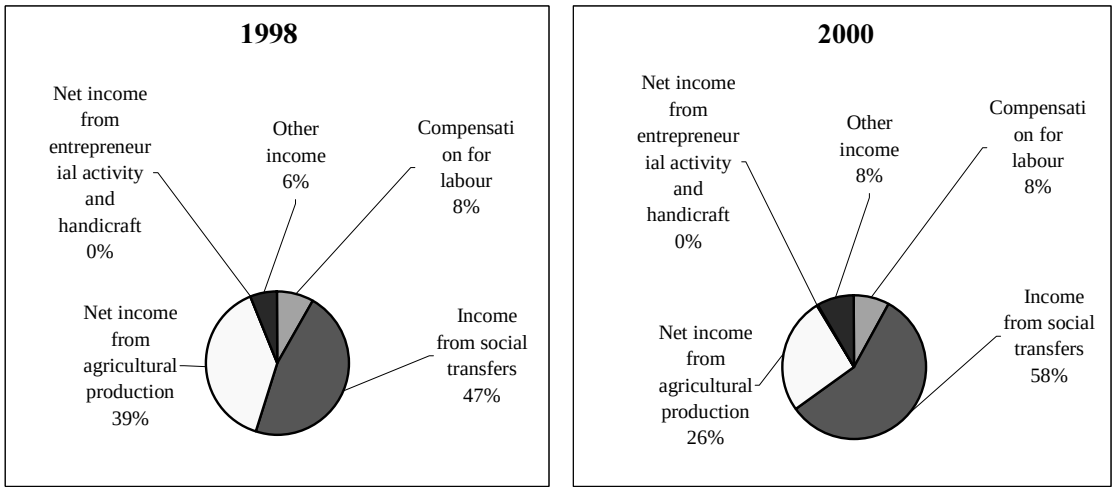


Source: The Household Budget Survey 2000.

The level of income in households of different socio-economic groups is different. The income was close to the average in households of wage and salary earners, while the level was under average in households of farmers and pensioners, as well as in households without a regular source of maintenance.

Analysing the disposable incomes of farm households, the main source of income is net income from agricultural production and income from social transfers. During the last years, the share of net income from agricultural production in the budget of farm households decreased. It must be recognised that, in 1998 and 2000, the largest source of income in farm households was social transfers, not net income from agricultural production. And the share of income from social transfers in farm households is increasing (Figure 5.). It means that agricultural production loses the character of commodity production, and, in many cases, it is just practised to meet household consumption.

Figure 5. Structure of disposable income of farmers' household in 1998-2000, %



Source: The Household Budget Surveys.

Income objectives in Latvia

One of the priorities of the Latvian Government is: balanced development of Latvia's regions and a high-level of employment. To this end, the government and the parties comprising this government will be committed to the policy, which is to ensure the provision of balanced development of the social and economic environment in the country, increasing the number of working places, reducing the unemployment and fostering of personal income. The government has a fixed objective, which is linked with increasing income. However, this objective also gives responsibility to every person because from one side the government encourages employment in the state, but from the other side, the Latvian population should also take care of their income.

Other objectives are also determined in the Law on Agriculture, which sets the objectives for income development. One task of this Law is to create preconditions:

- To justify average annual income from agricultural production and processing with the average annual income of the national economy.

- To compensate agriculture for conditions created by nature and economic factors, which are more unfavourable, compared to other industries in the national economy, providing equal social and economic welfare opportunities to the population employed in agriculture.

Instruments and efficiency of state policy

There are two types of policy instruments to increase the income of agricultural and rural households. One is a direct instrument, which is agricultural support for farmers. According to the operating results of agricultural producers in 2001, the production subsidies comprised about 53% of total amount of support on average. About 8% of total support was subsidies for investment in statutory companies and 17% in individual farms. At the same time, a considerable share of the total amount of state support was reimbursement for excise tax for diesel fuel for both types of agricultural

producers (statutory companies and individual farms) - it was about 25%, which is one of the most important instruments in the taxation system for agriculture.

The second set of instruments are on indirect support of income. As mentioned above, the government is fostering employment using several instruments and giving possibilities to get more income. There are several indirect instruments used to increase income, these are mainly policy instruments promoting employment in Latvia. For example, credit programmes are aimed to give the possibility to extend or optimise production, or start new business activities, which also promotes the creation of new jobs. In Latvia, there are several credit programmes, for example:

- **Agricultural Long-term Investment Credit Programme** – it was adopted by the government in 2001 and was started in the Spring of 2002, which is mainly aimed at creating a long-term financing offer acceptable to agricultural holdings, expediting the attraction of investment for creation of farms of optimum size and enhancing the competitiveness of agricultural holdings. The Programme is aimed at making cheaper loan facilities available to Latvian farmers. This form of credit was particularly fostered by implementation of the subsidy programmes and SAPARD for the development and technological modernisation of agricultural production, which gave rise to the demand for loans on the part of farmers.

- **Agricultural Land Acquisition Credit Programme** – it began to operate in July 2002. The Programme is aimed at launching the mechanisms for efficient functioning of agricultural land markets by supporting the development of competitive production areas meeting the European Union standards and the consolidation of lands in order to encourage an efficient cultivation of agricultural land. This Programme is planned for the granting of long-term (15-25 years) loans for the acquisition of agricultural land. It is possible to receive loans under this programme at an annual interest rate of 4%.

- **Non-agricultural Business Development Programme** – it was adopted by the government at the end of 2002. This Programme started to operate in 2003. The overall aim of the Programme is to facilitate the economic development in rural areas by supporting non-agricultural businesses, improving the infrastructure, improving the rural landscape to meet the business requirements and observing environmental protection requirements.

- **Loan Guarantees for Rural Businesses -** State-stock Company Rural Development Fund has been established, issuing guarantees for businesses – borrowers – in the event of insufficient loan security. A total of 466 loan guarantees for LVL 4.83 million were granted since 1997.

The relevant support comes also from **Foreign Financial Support for Rural, Agricultural and Forestry Development SAPARD**, which really started in 2002 after accreditation of the Rural Support Service (SAPARD agency) at the end of 2001. The SAPARD programme has several measures, which aim to increase the incomes of agricultural enterprises and to increase the competitiveness and farming income level, to increase the competitiveness of the processing sector and its compliance to EU requirements is the objective of this priority and to create employment and a more diverse employment structure in the rural territory.

To estimate the efficiency of these instruments is difficult at this moment, due to a lack of information at the microeconomic level for 2002. Many of the above mentioned instruments were started in 2002 or later and therefore real effects could only be identified at a later stage. At the same time, analysing the average monthly wage and salary in agriculture, it is possible to see that incomes in agriculture have been increasing in the last years. It proves that the situation of agricultural and rural

incomes is improving. The reasons for this increase in incomes could be the effects of both agricultural support and credit programmes and the economic development in Latvia.

Conclusions

Summarising the results of the study on income trends and state policy, it is possible to underline several conclusions on the situation of agricultural and rural incomes:

- The average monthly salary in agriculture was about 60% of the average monthly wages and salaries in the whole economy and the average monthly wages and salaries in agriculture, hunting and forestry was about 77% of the average salary of the economy in 2002. The proportion of the average monthly wages and salaries in agriculture has been increasing since 2001.

- The average income per employed person in agriculture has also been increasing annually since 2000.

- The main source of disposable income of farmers' households is net income from agricultural production and income from social transfers.

- During recent years, the share of net income from agricultural production in the budget of farmers' households decreased. And the share of income from social transfers in farmers' households is increasing. It means that agricultural production loses the character of commodity production and in many cases, it is just practised to meet household consumption. And it also shows that the employed population in agriculture is ageing.

- In rural areas the net income of agricultural production forms about 12% (in 2000) of all disposable household income. However, net income from agricultural production continued to decrease.

- The highest income level was in households in the Riga region. In other regions household income was lower than average income in the country. In the Latgale region, the disposable income was about 71% of average income in the country in 2000.

- The net farm income is higher in farms with 8-40 ESU. The inconsiderable net added value is in small size farms, in the group of farms from 1 to 4 ESU, which shows that production effectiveness start to increase at certain production levels.

- The government has fixed objectives, which are linked with income increases, but these objectives also give responsibility to every person because from one side the government encourages the employment in the state, but from the other side the Latvian population should also take care about their income.

- One of the policy instruments with which the government fosters an increase in agricultural and rural households is agricultural support for farmers. The production subsidies comprised about 53% of the total amount of support, on average, in 2001.

- Several instruments are used to increase income, which are mainly policy instruments promoting employment and giving possibilities to extend or optimise production, or start new business activities, which also promote the creation of new job places in Latvia.

GLOSSARY

A household – a person or a group of persons tied by a relationship or other personal relation, having common subsistence expenditures and inhabiting the same living unit (house, flat, etc.), the maintenance of which is covered by such persons jointly.

The disposable income of the household – is the sum of income in kind and in cash, that the household has received after settlement of taxes and other compulsory payments and can be used for consumption, other needs and accumulation. It consists of wages/salaries and other income for work, social transfers, "net income" from entrepreneurial activity, domestic craft or agricultural production and other income (gifts, alimonies received, income from the sale of property, etc.).

Social transfers – consist of the sum of money that is paid in the form of pensions, scholarships, social insurance and protection, social aid from the local government, as well as material assistance (in money and kind), granted by the local governments, human and social aid agencies, alimonies and financial aid, etc.

Farm household – conditionally includes also these households where the main breadwinner is a pensioner with more than 1 ha of arable land, if these households comprise able-bodied household members.

Agricultural farm – an economic and technical unit having common management, common means of production and labour force for the production of agricultural products.

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INCOME AND INCOME DYNAMICS OF THE LITHUANIAN RURAL POPULATION AND FARMERS BETWEEN 1996-2001

Part I

By Ms. Grazina Jalinskiene and Dr. Donatas Stanikūnas

The agricultural reform in Lithuania, launched after regaining the country's Independence, met the expectations of the rural population only in part and at the same time created preconditions for serious economic and social problems such as emerged and growing unemployment, exposed income differentiation and, finally, the highest poverty scale ever. In recent years Lithuania has seen worsening records of the persons engaged in farming; that is, decreasing income per family member, on the one hand, and a dwindling share of work income in the total income structure of the households, on the other hand. Accordingly, the need for social assistance has been rising.

Data for 2001 suggest that 54 per cent of a rural household's average income was spent on food, and only rural households attributed to decile X spent less than 50 per cent of total consumption expenses on food. The disposable income of the rural households accounted for 76 per cent of the disposable income level of the nation's households and for 68 per cent of that of the city households, as well as 61 and 51 per cent of cash income respectively. The disposable income of farmer households formed just 61 per cent of the nation's average, 55 per cent of the city level, and 80 per cent of the rural level, whereas the farmers' cash income formed 38, 33 and 63 per cent respectively.

As EU integration gathers momentum, besides the issues of investment assistance to agriculture restructuring, the social low-income issue must be addressed intensively, particularly in the light of waning skills among most residents to earn their living on traditional farming activities. The farmers who make a living on their land plots of 2-3 hectares fall under the group of the poorest and socially most vulnerable population.

The income level and structure of Lithuania's rural residents, including farmers, like that of all the population, is determined by demographic, socio-economic and other conditions.

The Lithuanian population census (2001) data showed an increase in the nation's rural population share from 32.3 per cent (data of the 1989 census) to 33.1 per cent. The rural population's growth was buoyed up by the increased migration of city residents to the countryside as the natural increment of the rural population has been negative since 1991. The city residents who have lost a job and failed to find an income source in a city revert to small-scale agricultural production as a subsistence option that does not require big efforts (knowledge and employment) or substantial resources, which is why it is seen as a generally accepted economic activity. In 1991-1996 the number of residents engaged in farming and their share in the total number of employed residents across the country had surged by around 18 per cent. Since 1997 the number of persons working in the agriculture sector and their share in the country's total working population has dwindled. At this point every fifth employed resident of Lithuania works for the agriculture sector (as compared to approximately every sixth resident working in the processing industry, and every seventh in the commerce field).

Another difference between the countryside and the city concerns the population's age structure. One can observe a notable ageing process in the rural population – since 1990 old people have outnumbered children in the countryside as the rural ageing index grew from 103 to 109 in the period 1990 through 2001. The residents who are 60 years of age and above constitute 23 per cent of the rural population, whereas in the cities the figure stands at 17 per cent.

Since 1990, the countryside has witnessed a declining birth rate. In 2001 the rural birth rate slumped 39 per cent compared to 1990. Though the pace of decline in birth rates between the city and the countryside is similar, the latter still can boast a higher birth rate than the cities. Data for 2001 indicate a 23 per cent bigger rural birth rate per 1 000 population versus the city.

It is a difficult task to single out plainly the statistical socio-economic group of the residents engaged in agricultural production. The statistics on national accounts and household budgets, in the farmer category, list those households that gain the bulk of their income from agricultural activities. The statistics on employment reflect a similar picture. In the social insurance system the key criterion is the existing registration of a farm, while in social assistance the main criterion is the land area in use. The policy for agriculture and rural development is based on the criteria of the percentage of cultivated land area, animals, homemade agricultural production and services provided to agriculture.

In Lithuania, data from the Household Budget Study serve as the principal source for research into the income level, structure and dynamics of rural residents and farmers. In the analysis of farmers' income level and differentiation, the two following criteria are applied to identify farmers in the whole group:

- Criterion of agriculture as the major source of income.
- Criterion of land area in use (or agricultural activity). Among the overall data of household budget studies a group of rural residents engaged in farming to a lesser or greater extent is singled out. This group comprises two sub-groups: households for which farming is 1) a major source of income, and 2) an additional source of income.

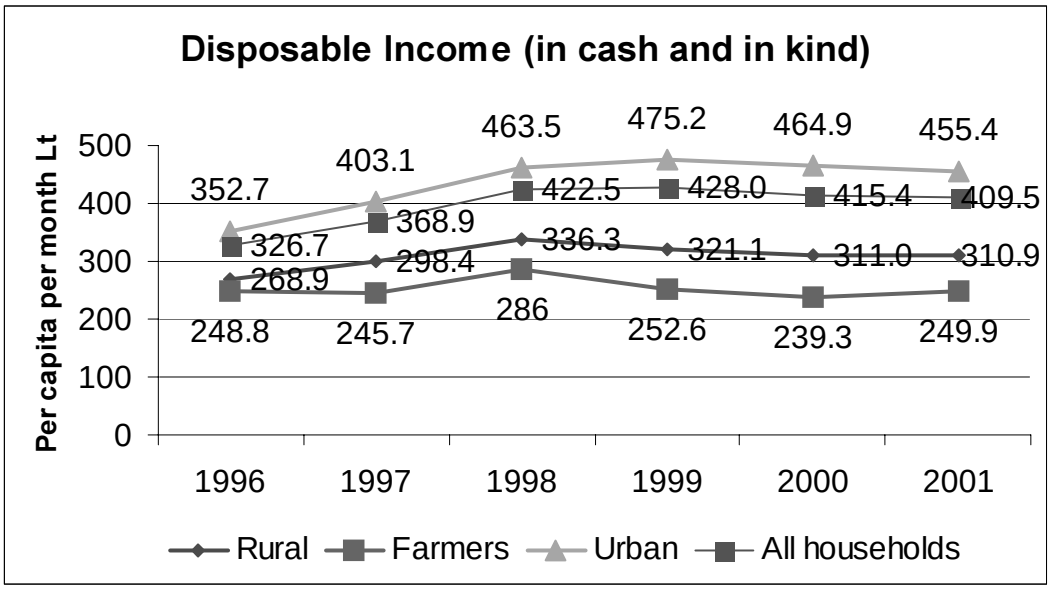
Based on the data of the Household Budget Study, households whose major income source represents income from a private farm accounted for 18 per cent of all rural farms in 2001. As many as 40.3 per cent of the rural residents said their income from a private farm represented an additional source.

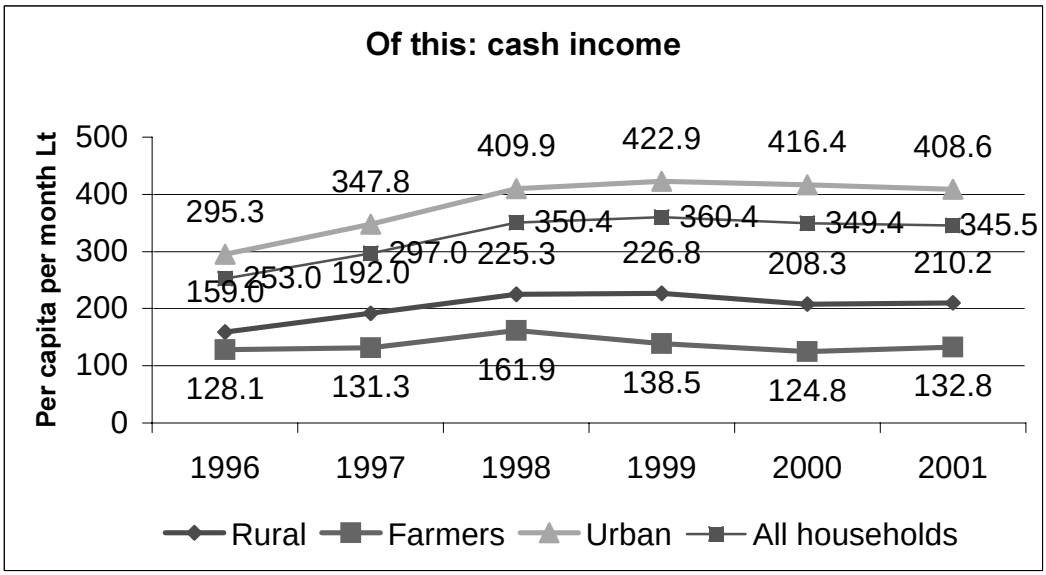
Income level, structure and dynamics of the rural population and farmers

Different pace of economic development leads to varying income levels between the city and the countryside. The disposable income of rural households is significantly lower as compared to that of urban households. Regional disparities in income continue to grow. In 2001 the real total disposable (cash and in-kind) income of the rural population dropped 2 per cent compared to 1996, as opposed to a 9.4 per cent surge in the income of the urban population in the period. According to the Household Budget Study, the average statistical level of farmers' income is well below the national average, whether in the countryside or in the city (Figure 1).

Figure 1. Average disposable income of households

(farm households where agriculture is major source of income)





Source: *Income and Expenditure of Households in 1996-2001*, The Lithuanian Statistics Department.

The income gap between the city, countryside and farmers broadened in the years 1996-2000. In 1996 the average monthly disposable (cash and in-kind) income of rural households per household member formed 82 per cent of the nation's total income and 76 per cent of urban households' income, while in 2000 the percentage was 75% and 69% respectively. The disparities in cash income are even sharper, *i.e.*, in 1996 the monthly cash income of rural households per household member amounted to 63 per cent of all households' level and 54 per cent of respective income in the cities. In 2000 the figures stood at 60 and 50 per cent respectively. A year later, this gap between disposable incomes shrank modestly to 76 per cent versus the national income level, but rose to 68 per cent versus the city, while the gap between cash income levels slightly narrowed to 61 and 51 per cent respectively.

In 1996 the average monthly disposable (cash and in-kind) income of farmer households per member constituted 76 per cent of the national total, 92 per cent of the rural level and 71 per cent of the urban level. The figures for 2000 were 58, 77 and 51 per cent respectively. In 2001 this gap, though, dwindled to 61, 80 and 55 per cent respectively. The cash income gap among the aforementioned population groups is even broader. In 1996 the average monthly cash income of farmers per household member made up 51 per cent of the income level of all households, 81 per cent of the rural level, and merely 43 per cent versus the cities, whereas in 2000 the figures were 36, 60 and 30 per cent respectively. One could observe a modest reduction in this gap to 38, 63 and 33 per cent respectively in 2001.

Farmers earn significantly less income compared to that of other economically active population groups across the country and in the countryside (Figure 2).

Figure 2. Disposable income by socio-economic groups of households in 2001

S*ources: Income and Expenditure of Households in 2001*, The Lithuanian Statistics Department, 2002. Data of the Household Budget Study, The Lithuanian Statistics Department.

The disposable (cash and in-kind) income of farmer households in Lithuania was 45 per cent lower in comparison with that of workers hired in other sectors than agriculture and 44 per cent lower versus the income of business persons (self-employed persons, employers) in 2001. The gap between cash income was even wider posting 67 and 66 per cent respectively. Furthermore, the average income figures of farmer households were notably lower as compared to the average income of households of retired persons, namely 31 per cent below the total disposable income, and 55 per cent below the cash income.

The countryside also shows a big gap between the income of "statistical" farmer households (see Figure 2 which includes a rural household chart) and other social groups of the economically active rural residents, in particular as regards cash income. In 2001 the total disposable income was 33 per cent below that of rural business persons and 27 per cent below the income of workers hired in other sectors than agriculture, while cash income was 54 and 47 per cent lower respectively.

Income (expenditure) differentiation between rural residents and farmers

The differentiation between the consumption levels of rural households has tended to decrease, which results from a bigger growth of the lowest consumption level rather than that of the highest consumption level. The consumption expenditure of the richest rural households (decile X) per capita exceeded 8.2 times that of the poorest households (decile I) in year 1997, and was 7.8 times higher respectively in 2001. The richest households boosted their consumption expenditure by 3.6 per cent and the poorest households by 9.3 per cent over the period.

For estimation of the farmer income differentiation, the selection in the household budget study is insufficient, where the farmer group encompasses the households[1] whose major source of income is agricultural activities in a private farm. Such a type of selection can be helpful only for the assessment of the "average statistical situation" because a narrow selection affects data reliability, in particular in research into the budgets of residents forming a small group in society.

Among farmers, like other socio-economic groups of the population, one can observe large income gaps. In order to eliminate the selection insufficiency problem as much as possible and analyse the income differentiation among farmers and the poverty spreading level by size of farm, the household grouping is applied based on the two aforementioned criteria (the criterion of agriculture as a major source of income and the criterion of land area in use (or agricultural activity).

Based on the area of cultivated land in a farm, the households' disposable income disparities in the socio-economic group of farmers (where farming is major source of income) were consistent in 2001. The total disposable income from small-scale agricultural production in farms of up to 3 ha was twice below the income of larger farms of above 10 ha. The cash income disparities were even more vivid (Figure 3). On the other hand it should be noted that in the household budget study the households using up to 3 ha of land and earning core income from agricultural activities accounted for a mere 7 per cent of the "statistical" farmers. The rest of the respondents (93 per cent) using a land area of up to 3 ha had other (major) sources of income, namely 49.5 per cent received income from hired labour, 44.9 per cent from pensions, 2.5 per cent from self-employment (other than agricultural business), and 3 per cent from other sources (benefits, property, grants etc). Figure 3 shows notable disparities in the average disposable income levels in the group of up to 3 ha between the households with agriculture as a major source of income and the households earning money from agriculture as an additional source of income.

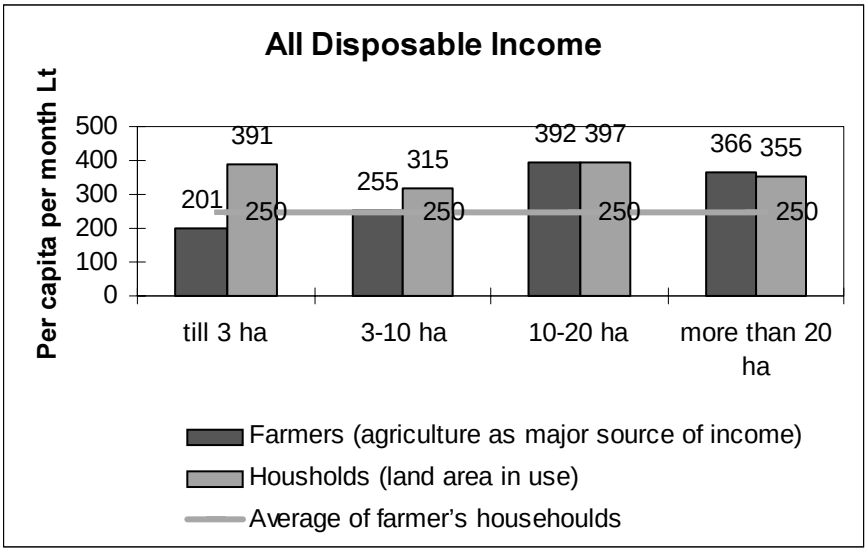
In other respondent groups with land areas above 3 ha, the above disparities between disposable income levels were minimal.

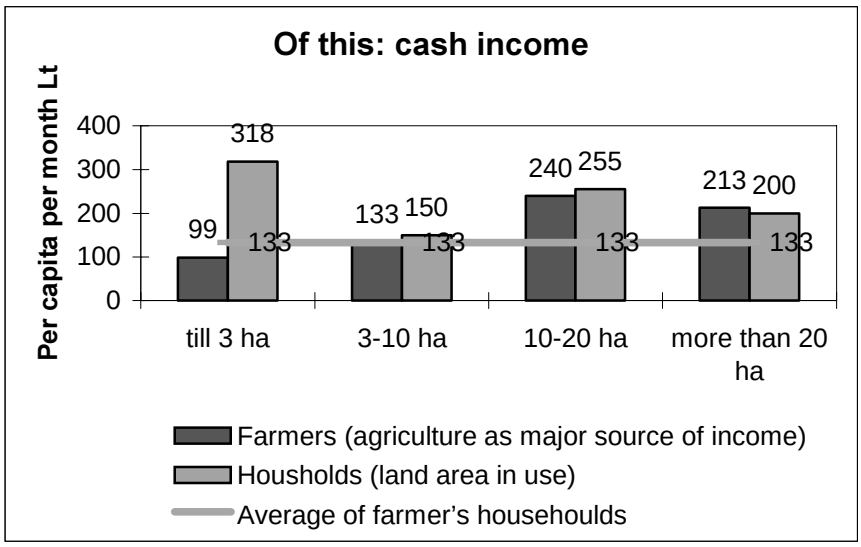
In farmer households with a land area of above 10 ha, the average disposable income amounted to 94 per cent of the national average and was 24 per cent above rural households' average in 2001. But their cash income level constituted only 69 per cent of the national average. In-kind income accounts for a large share in this income group. It should be noted that in the respondent group concerned, 57 per cent represented households engaged in agriculture as the core source of income, and the rest - as extra sources. The breakdown by socio-economic status was as follows: 52 per cent represented farmers, 19 per cent – hired persons in non-agricultural sectors, almost 26 per cent - pensioners and around 2.5 per cent – households of self-employed persons or businessmen in non-agricultural sectors.

1. In the 2001 *Household Budget Study* the socio-economic group of farmer households constituted a meagre 5.7 per cent of all households included in the study, or around 450.

According to data in Figure 3 and in view of the socio-economic composition of the respondents under 3 ha and those above 10 ha, the conclusion may be drawn that the worst situation appears in the group of low-income households between 3 and 10 ha. In 2001 their average disposable income made up just 62 per cent of the national average and 82 per cent of the rural income level, while their average cash income stood at 62 per cent below the national average. Over 31 per cent of respondents in this group were involved in agriculture as the key source of income and even 68 per cent – as additional source of income. A majority of these, or 42 per cent, represented households of retired persons.

Figure 3. Disposable income by groups of land areas used by households in 2001





Source: Data of household budget studies, The Lithuanian Statistics Department.

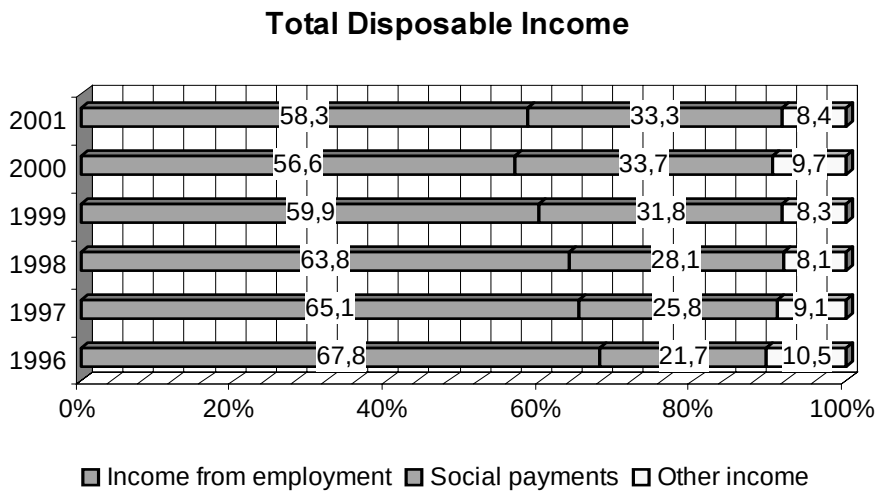
A comparison of the research results into income disparities between households engaged in agriculture with the conclusions of the expert group which drafted the National Poverty Reduction Strategy show that disparities in the income levels of the Lithuanian population exceed those in other European states (the Gini coefficient, reflecting income concentration level, calculated according to average annual income per capita, increased from 0.23 in 1987-1988 to 0.37 in 1993-1995, a figure which exceeded the average of Central Europe, except the Baltic region,[2] *a priori* leads to the conclusion that among candidate states, Lithuania has got the widest disparity in income and life quality levels of the rural population, in particular, farmers.

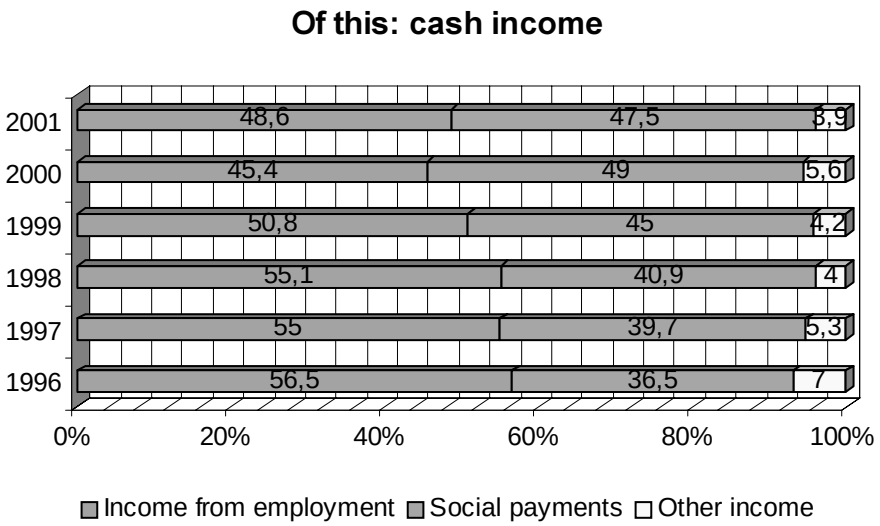
Income structure of rural residents and farmers

The share of work income of rural residents increased in the years 1996-1999, but later showed a tendency to decrease. The share of social benefits in total disposable income of rural residents tended to narrow since 1996 and in the period concerned, the share of social benefits in the cash income of rural households increased by 10 percentage points, *i.e.*, from 36.5 per cent to 47.5 per cent (in 2001 versus 1996).

2. *The National Poverty Reduction Strategy*, The Ministry of Social Security and Labour, UNDP, Vilnius 1999. *Poverty in Lithuania: Capacity Building for Poverty Reduction in the Countryside*, R. Lazutka, O. Katsiaouni and J. Gorniak, UN Development Programme, Vilnius 2000.

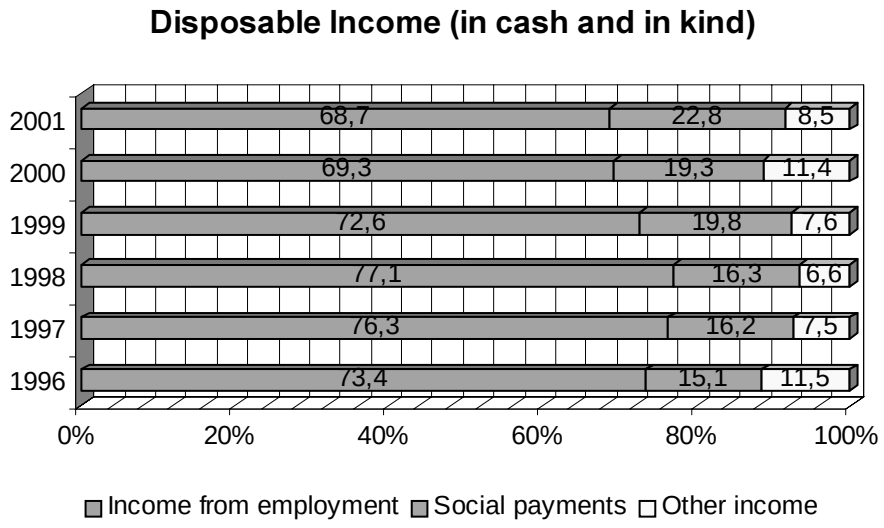
Figure 4. Income structure of the rural population in 1996-2001

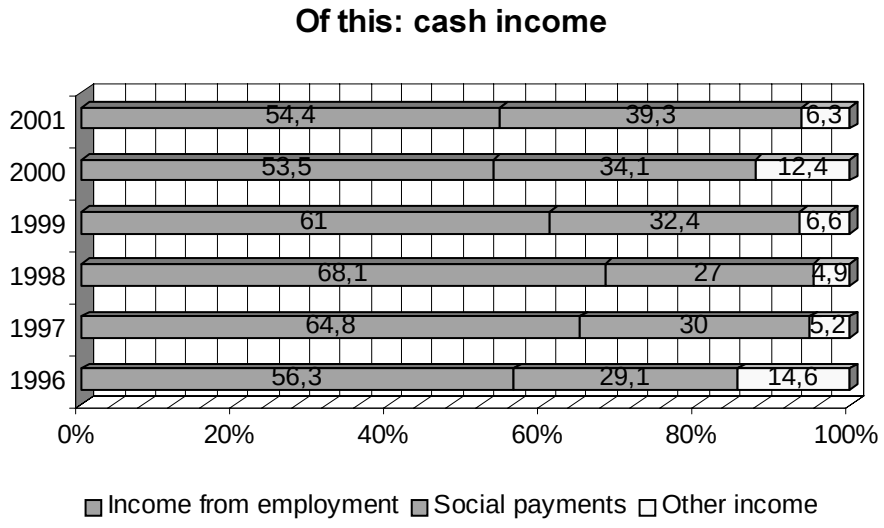




The share of benefits and other social payments in disposable income of farmer households (particularly cash income) tended to grow, whereas the share of work income showed a tendency to decline (Figure 5).

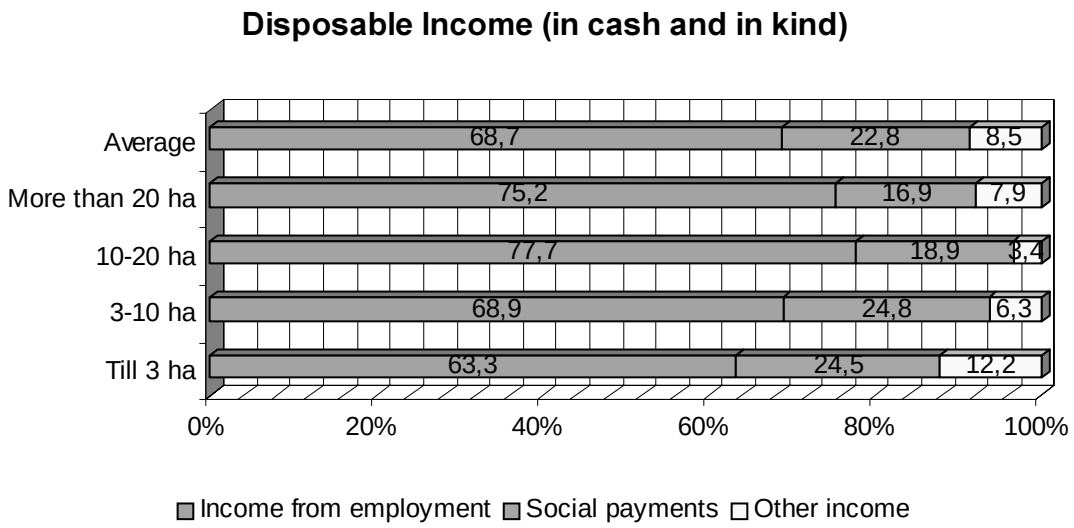
Figure 5. Major income sources of farmer households (where agriculture is the major source of income)

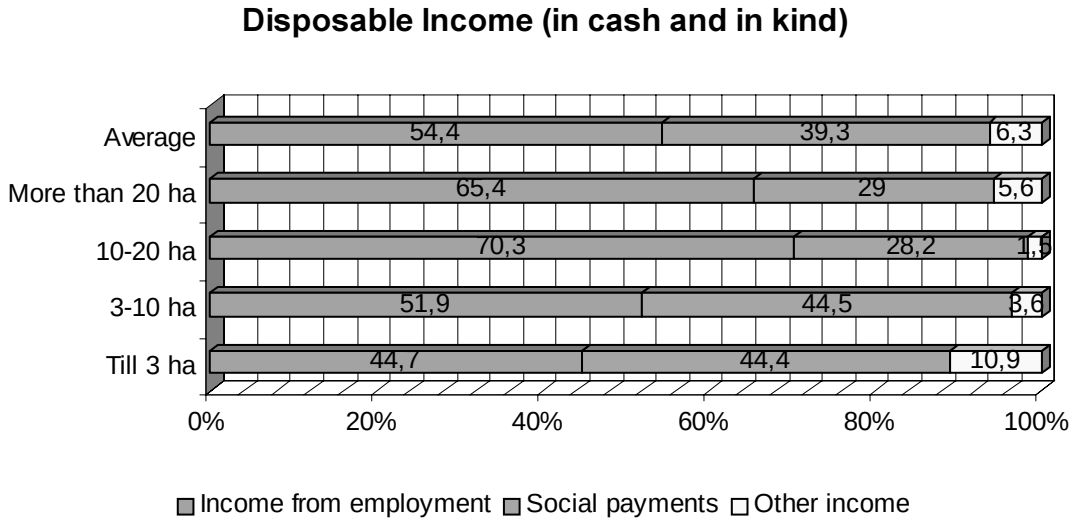




Over the recent six years, the share of various social benefits in cash income of households broadened by over 10 percentage points from 29.1 per cent in 1996 to 39.3 per cent in 2001. Such a tendency is indicative that the living standards among an increasing number of persons related to agriculture depend on social benefits. There are an increasing number of social benefit recipients in the group mentioned, with less work income recipients. This means a prospect of continued poverty growth and aggravating burden of assistance to the economically active part of society.

Figure 6. Major income sources of households by groups of land area use d by farmers (where agriculture is a major source of income)

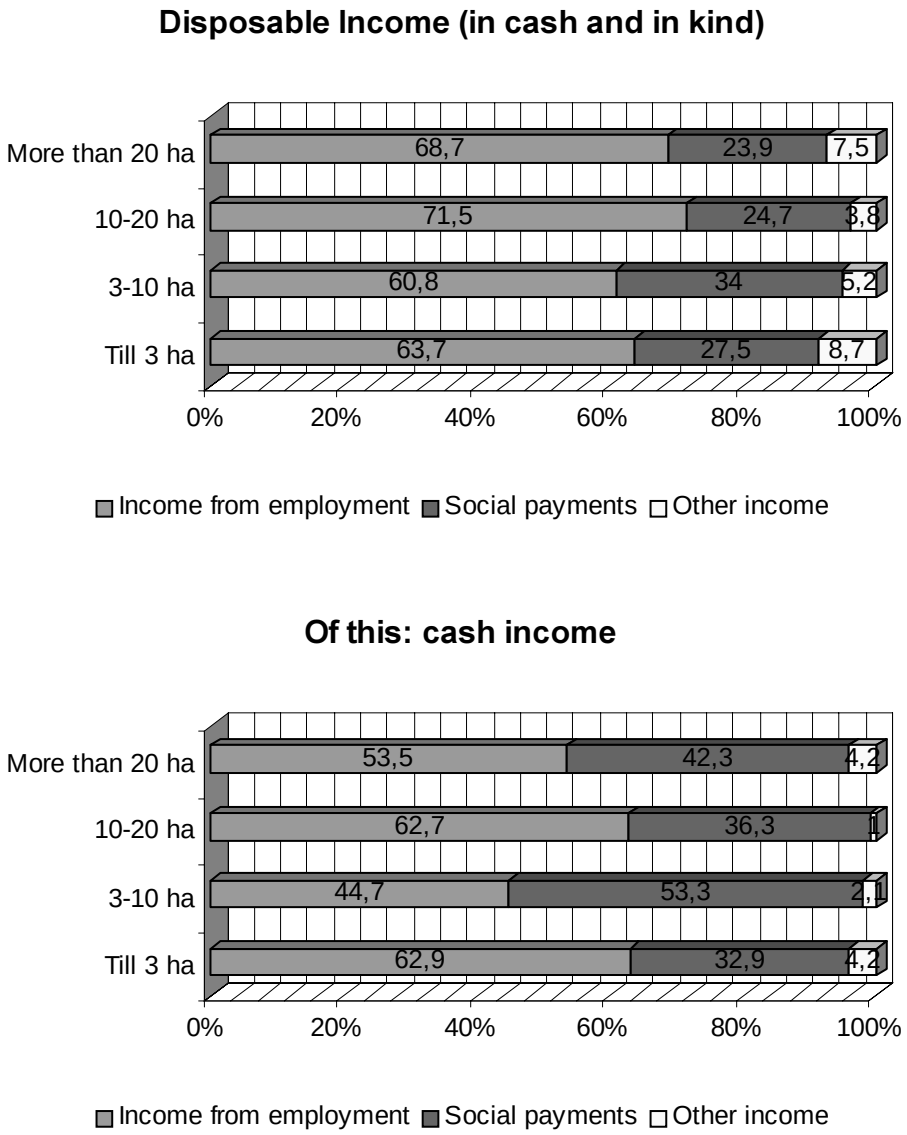




Source: Data of household budget studies, The Lithuanian Statistics Department.

On the other hand the ratio of work income and social benefits vary largely between farmer households of different agricultural activity. In 2001 social benefits represented the bulk of the budget, 45 per cent, in small farmer households under 10 ha with the lowest income. In family budgets of farmers running above 20 ha, by contrast, the work income was twice the share of social benefits.

Figure 7. Major income sources of households cultivating land

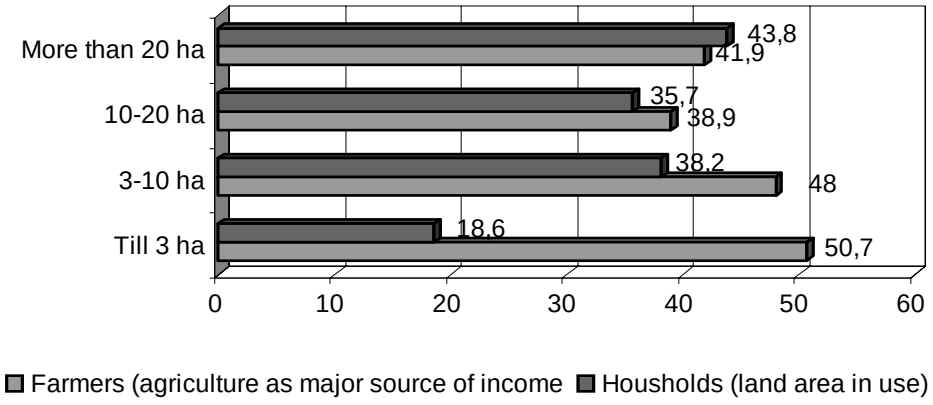


S*ource:* Data of household budget studies, The Lithuanian Statistics Department.

It should be noted that in-kind income accounts for a greater share in the household budget of most farmers (in all groups of cultivated land areas). Foodstuffs produced for own needs form the bulk of in-kind income.

The in-kind income from agriculture represents a guarantee for most rural families to achieve a certain living standard, at least sufficient nourishment. But such income, though substantial, does not offer people the freedom of choice as cash income does, and thus further narrows personal needs. Therefore, households with small cash incomes are more economically and socially vulnerable, even though these create a more or less bigger in-kind income.

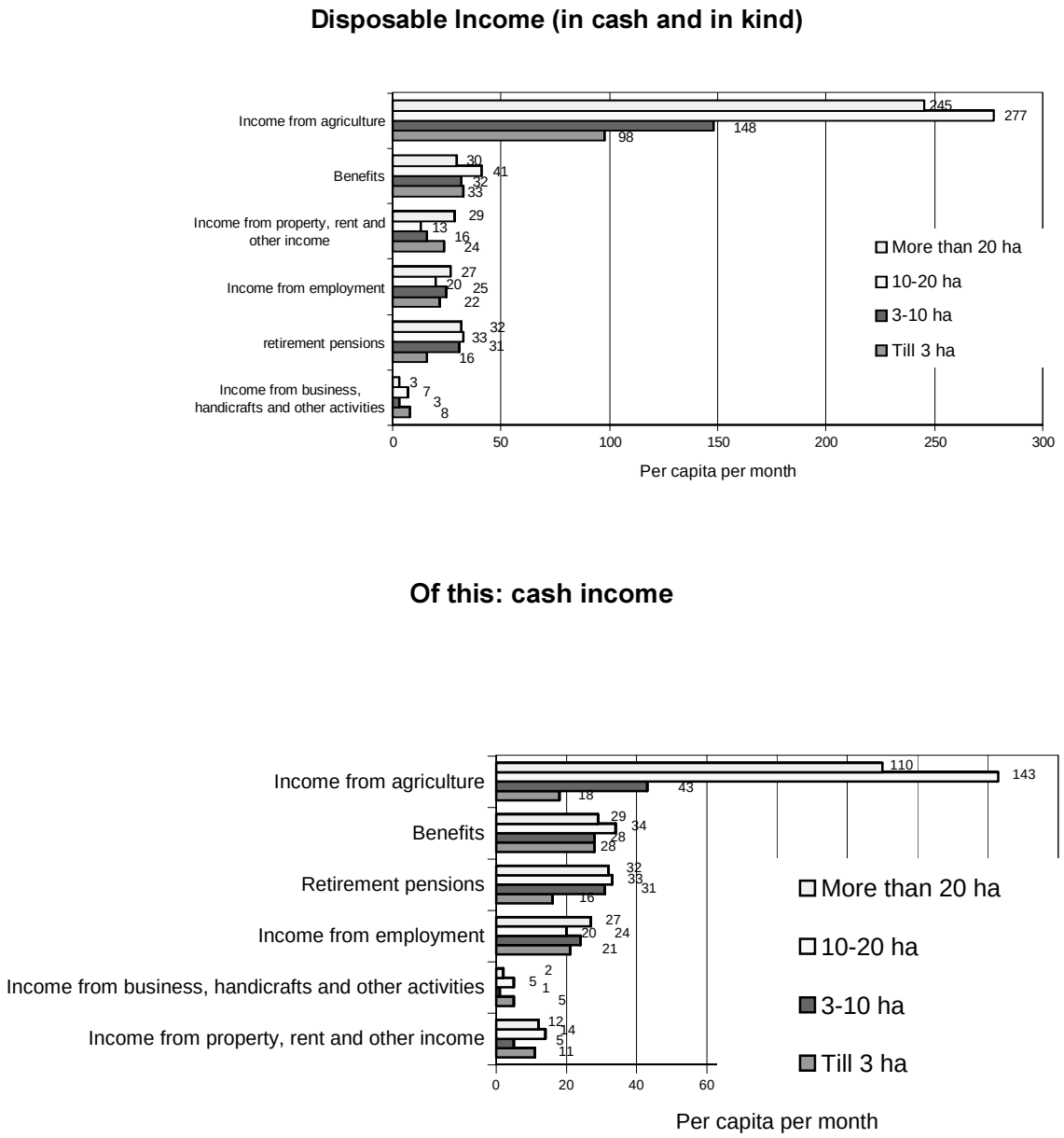
Figure 8. Share of in-kind income from agriculture in the disposable income of rural households (per cent)



Source: Data of household budget studies, Lithuanian Statistics Department.

Besides, it should be added that cash income from agricultural activities in small farms is either very modest (*e.g.* in 2001, the major monthly income from agricultural activities (Figure 9) was between 18 Litas per member on farms of up to 3 ha, and a negative sum (monthly additional income of -8.07 Litas per member from agricultural activities on farms), *i.e.* where investment in agricultural production exceeded the return on the sale.

Figure 9. Disposable income of farmer households where agriculture was the major source of income in 2001



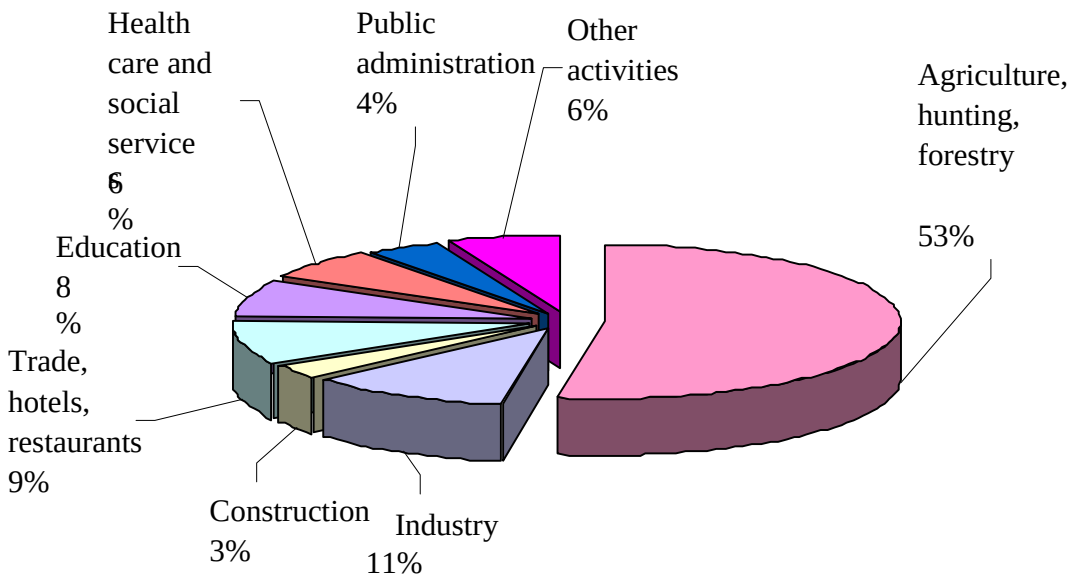
S*ource:* Data of household budget studies, The Lithuanian Statistics Department.

A big effect of agriculture on income of the rural population is also proved by the results of many social studies. For instance, in September of 1997 during a special poverty and employment study, 37.3 per cent of the rural respondents identified agriculture as the major source of their income, whereas another 34.3 per cent indicated pensions, and 28.6 – work payment (Motiekaitienė V., 1998). A further study (1999) of the living conditions in Lithuania found that 30.5 per cent of rural households earned their major income from work in agriculture, and as much as 62.8 per cent survived

on various types of social benefits (old-age and other pensions, unemployment, child care, social and other benefits) (The Ministry of Social Security and Labour of the Republic of Lithuania, 2000). Besides, data obtained from the 1997 study of living conditions of social benefit recipients show that around 62.1 per cent of socially supported rural families are engaged in agriculture as one of the major income sources, in view of the fact that their major source of income is social benefits (The Ministry of Social Security and Labour, Vilnius University, Health Economics Centre, 1998). Hence, the predominant dependence of rural residents' income on agriculture as an income source remains, though to a lesser extent.

The working activity of many rural residents is still concentrated to agriculture. As of early 2002 this sector employed almost half of the officially working rural population (Figure 10). Alternative activities have not yet had any noticeable socio-economic impact. In the period 1996-2001 the income from non-agricultural business, crafts and free professional activities accounted for a meagre 1.9-2.8 per cent of the disposable income of rural families.

Figure 10. Distribution of employed rural residents in economic activities as of February 2002 (per cent)



Source: *Labour Force, Employment and Unemployment* (study data), February 2002, The Lithuanian Statistics Department.

The concentration of the economic activity of residents in agriculture reflects the outcome of not only the economic transformations that occurred in the first half of the 1990s, but also of social factors. First of all, this is a counteraction of residents to unemployment. It was not the rural residents alone, but also the city dwellers who, after losing a job and failing to re-orientate themselves and find a living source in the city, moved to the countryside to start farming in either large or small land areas. The living conditions of poor residents, social benefit recipients, exposed persons, once in a tough situation, to attempt to move to the countryside, forever or at least temporarily, in order to undertake agricultural production so as to ease their subsistence.

On the other hand farming does not ensure full employment to most farmers and does not provide sufficient income to their families to achieve an adequate living standard. Their income is lower compared to those employed in other sectors.

Based on data from the 1997 Poverty and Employment Study, over half (54 per cent) of those employed in agriculture earned up to 200 Litas and almost one-third (32.2 per cent) – up to 400 Litas in monthly cash income. According to the work payment records of the hired workers available in the Statistics Department, in the years 1996-1999 the average monthly work payment in agriculture, hunting and related services sector was 48-50 per cent below the national average pay, while agricultural companies reported even a bigger difference of 48-53 per cent.[3] Unfortunately, due to the lack of data accounting on farms, there are no available data about the income of farmers or their hired labourers. Therefore, at this point the income level in the group of farmers running their own farms or their hired labourers can be judged merely on the basis of household income studies. As mentioned above among the economically active rural residents, farmers have the lowest income and represent the most poverty-stricken group.

Poverty level in the countryside

Poverty research applies a number of indicators such as the poverty line, poverty level, poverty spread, poverty depth and other. To measure the poverty level, various poverty limits may be applied, which are usually established taking account of either minimum necessities (absolute poverty limit) or the achieved income (expenditure) level of residents and income differentiation (relative poverty limit).

Lithuania, on expert recommendation, has the practice of regarding a relative poverty limit as the basic poverty limit, *i.e.* 50 per cent of the consumption expenditure median per equivalent consumer (further a relative poverty limit). Re-calculation per equivalent consumer is done in order to eliminate the effects of household size and composition on the poverty indicators. In 2001 the relative poverty limit constituted 265 Litas per capita per month. According to data of the household budget study, consumption expenditure below the poverty limit was attributed to 16 per cent of Lithuanian residents, with the top poverty level of 27 per cent recorded in the countryside, and the lowest one of 8 per cent seen in major cities. Rural residents accounted for 53 per cent in the poverty-stricken population (32 per cent in the total population).

Farmers are numbered among the most vulnerable residents, since the poverty level in this group was the highest standing at 35 per cent, *i.e.* twice as big as the national average poverty level and more than thrice the poverty level in the urban population.

What are the causes of such a high poverty level in the countryside? The main one is the high unemployment level that posted 15.9 per cent at the beginning of 2003 (the national average was 10.9 per cent). The rural unemployed accounted for over one-third of all the long term unemployed, of which most are male jobless persons. Every fourth long term unemployed rural resident has an unemployment record of above 2 years.

The employment level in the countryside fell from 59.5 per cent in 1998 to 44.9 per cent in 2001, 5.8 per cent below the city level. The lower income level among rural residents versus the cities was due to lower productivity. Albeit agriculture employs approximately 17 per cent of the total workforce, this sector creates merely 7 per cent of the domestic product (GDP). The income level in rural households is also contingent on the fact that 60 per cent of such households have only one

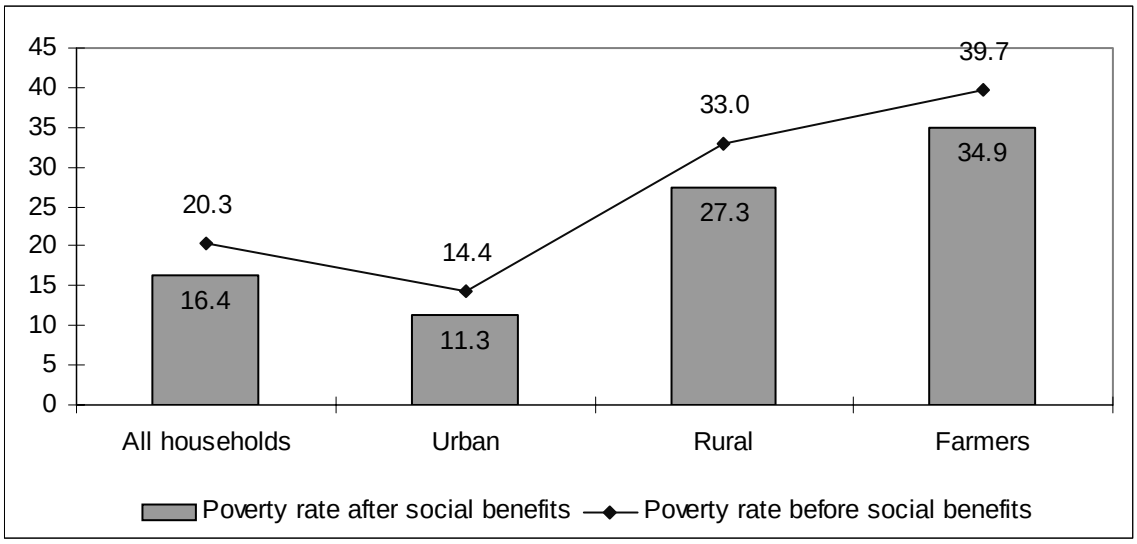
3. *The Lithuanian Statistics Chronicle*, 2001.

working member. Nearly 40 per cent of household heads in the countryside are 60 years old or older, with pensions as the major source of income.

To recapitulate on the causes of poverty in the countryside, it may be said that poverty in this sector arises from lower productivity resulting in lower income from the farm work, also joblessness, weak workforce mobility because of inadequate education and professional training, and negative developments in the income structure, *i.e.*, decreasing weight of work income and increasing weight of pensions and benefits in the income of rural and farmer households. The relative poverty among farmers in 2001, calculated after exclusion of social benefits, amounted to some 40 per cent, and that of rural residents – to 33 per cent (Figure 11).

Figure 11. Poverty level "before and after social benefits"[1] in 2001

(farmer households where agriculture is major source of income)



1. "Old-age and disability pensions, grants, sickness and child's care benefits were not attributed to the social benefits, by the amount of which the consumption expenditure was cut in measuring the poverty level 'before social benefits'."

S*ource:* Data of household budget studies, The Lithuanian Statistics Department.

Social benefits had varying effects on the poverty level of different resident groups. These benefits reduced the average poverty level, by 5.7 percentage points in the countryside, by 3.1 points in the cities, and the national average by 3.9 points.

Conclusions

1. The disposable income of rural households is significantly lower compared to the income of urban households. Regional income disparities continue to grow. The total real (cash and in-kind) disposable income of rural residents dropped 2 per cent between 1996 and 2001, which contrasts with a 9.4 per cent rise in the income of urban residents.

2. Poverty in the countryside originates from a lower work productivity that gives rise to lower income from private farms, joblessness, and weak workforce mobility due to inadequate education and professional training.

3. Farmers represent the most poverty-stricken socio-economic group both across the country and in the countryside. Poverty mostly endangers households that run a small farm of up to 10 ha and have no other major source of income. In 2001 the relative poverty level among farmers was 35 per cent, a rise of 8.6 percentage points since1996.

4. The share of benefits and other social payments in the disposable income of rural residents and farmers' households, particularly in the cash income, is widening every year. The existing social assistance system scales down the poverty level among farmers but the increasing share of social benefits signals an emerging dependence of an increasing part of the agriculture-related population on social benefits. There is an increasing number of social benefit recipients in this group, with less persons receiving work income.

5. Slowly developing alternative activities (rural tourism, herb and spice plant growing, production of organic products, various types of services etc) do not pave the way to an increase in employment in the non-agriculture domains in the countryside. Rural residents without entrepreneurship capacity, shortage of skilled workforce, weak business infrastructure, and unfavourable credit conditions aggravate job creation in the sectors of untraditional activities and small and medium-sized businesses. In addition, territorial workforce mobility is poor and few rural residents try to find a job in the adjacent cities.

6. In-kind income accounts for the bulk of budgets in the households of most farmers, irrespective of a cultivated land area. For many small farmers, such type of income is one of the guarantees for a certain living standard or at least sufficient nourishment. But such income, though substantial, does not offer people the freedom of choice, as does cash income.

7. Large income disparities exist among farmers, just like among other socio-economic groups of the population. The most affected are low-income farmer household groups with land areas between 3 and 10 ha, whose disposable income is nearly half of the income of the farms larger than 10 ha.

8. The general profile of the poorest farmers-social assistance recipients:

   – Persons with agricultural professions, who previously had worked for agricultural companies, and their families are most poverty-stricken in the countryside.

   – Nearly half of the farmers-social benefit recipients are between 30 and 39 years of age; the number of children is most abundant in this group, which is why the demand for social assistance is higher as compared to elderly persons.

   – A little more than half of the poverty-struck recipients of social assistance who cultivate land live in full families; on the other hand the social assistance system prompts farmers to live without registration of matrimony and in divorce, or to give birth and raise children in single-parent families.

   – Majority of the poverty-stricken farmers have no professional training and fail or have no access to re-training, which is why they undertake farming in land plots of 2-3 ha and get only short-term random jobs.

- Social benefits are paid to large families or single persons raising children. Almost one-third of them raise two children and less than one-third have 1-3 children. Nearly one-tenth of large families raise more than 5 children.

- Poor farmers predominantly choose cattle-breeding production, in particular dairying. A small part of minor farmers produce dairy products, breed pigs and cattle for meat not only for their own needs, but also for the market, and grow the traditional plant products such as potatoes, crops and vegetables.

- Three quarters of rural residents that cultivate land and receive social benefits are set to proceed with agricultural activities, indicating possession of their own land as the main motivation.

- The major income source of social benefit recipients cultivating land is social benefits. Respondents indicate that income from the sale of agricultural products and from hired labour as equal in value, but less important than social benefits.

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Part II: INCOME CHANGES IN FARMS PARTICIPATING IN THE LITHUANIAN FADN SURVEY IN 1999–2001

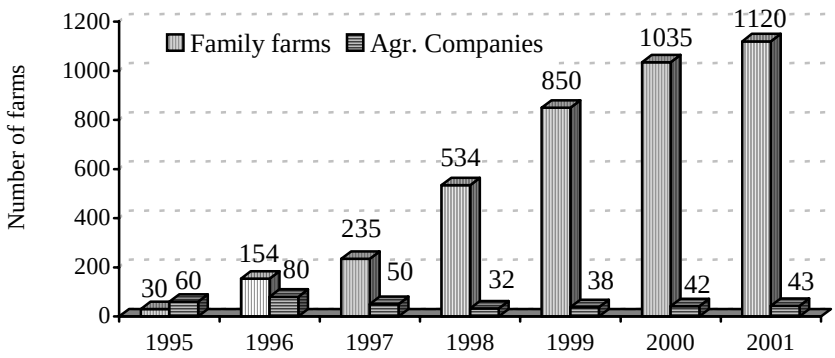
By Dr. Donatas Stanikūnas and Mr. Virgilijus Skulskis
(Paper presented by Dr. D. Stanikūnas)

This article handles the results of family farms participating in the Lithuanian Farm Accountancy Data Network (FADN) survey which is carried out according to the EU methodology. The main attention is paid to farmers' income. The precise structure of agricultural production will be known at the end of the year after processing the data of the Agricultural Census. However, the existing data allows us to draw certain conclusions. In 1999-2001 an increase in state support significantly influenced the growth of income on family farms. It set the preconditions for higher private consumption.

Analysis of income changes on family farms is based on the Lithuanian FADN database. The Survey of farming results according to the EU methodology were initiated in 1997. Some years before, similar surveys were undertaken, but they were rather limited due to the fact that very few farmers carried out book keeping. The number of survey farms started to increase rapidly when the FADN activities were clearly defined between LIAE and LAAS. The Agricultural Advisory Service not only advertises book keeping among farmers and assists in doing this job, but also collects FADN data and provides it to the Lithuanian FADN.

There are two main types of agricultural producers in Lithuania: family farms and companies. The structure of Lithuanian family farms according to the EU criteria (economic size and type of farming) is not yet known because the Agricultural Census will not be carried out until in June 2003. Therefore, farms, where farmers keep farming books and are willing to provide data to this system, are included in the survey so far. Concerning agricultural companies, the number of them is rather small and permanently declining. Companies, according to the EU criteria, are chosen to participate in the survey. Preliminary, 1 200 family farms and 45 agricultural companies from all Lithuanian districts participated in the survey of farming results in 2002. In this year about 40 thousand family farms were registered, therefore, the number of survey farms (approximately 3%) is sufficient to draw conclusions on farming results. The farmers, participating in the survey, produce almost 4% of total agricultural output. An average farm size among the registered farms is 15.2 ha. The small farms prevail, 40% of them are less than 10 ha. The paper covers a period starting from 1999, that is after the crisis in the Eastern countries, which had a rather significant influence on Lithuanian agriculture. From that year many farms were included in the survey.

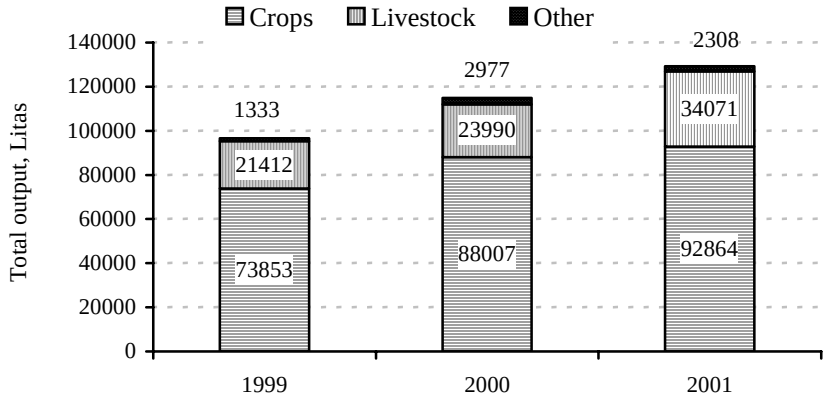
Figure 1. Dynamics of the Lithuanian FADN farms in 1995-2001



The structure of family farms included in the survey did not change in the course of the last three years. In the structure of the survey, family farms make up seven types of farming: two of them being crop specialization, cattle - dairying rearing and fattening combined, and different types of mixed farms. In 2001, like in 1999 and 2000, the largest amount of family farms (85.5%) belonged to farming types of specialist cereals, general field cropping, and mixed livestock, mainly grazing livestock.

From 1999 both total output and income from sales per farm rose. During 1999–2001 total output increased almost by 34%, income – 41%. Taking into consideration the decrease of prices in 2002, a presumption may be made that the farming results would decline. The rate of cost growth was sufficiently lower and during 1999–2001 it reached only about 23%. Income from sales exceeded paid costs, however, taking into consideration depreciation and the value of stuff produced and used in the farm, this difference in most cases would vanish. Rapid growth in income was the basis to increase expenditures for own consumption. In 2001 such expenditures exceeded 17 thousand Litas per family farm. Crop production prevailed in both total output and income from sales. In 2001 output crops accounted for 72% of total output and 76.5% in 1999 and 2000.

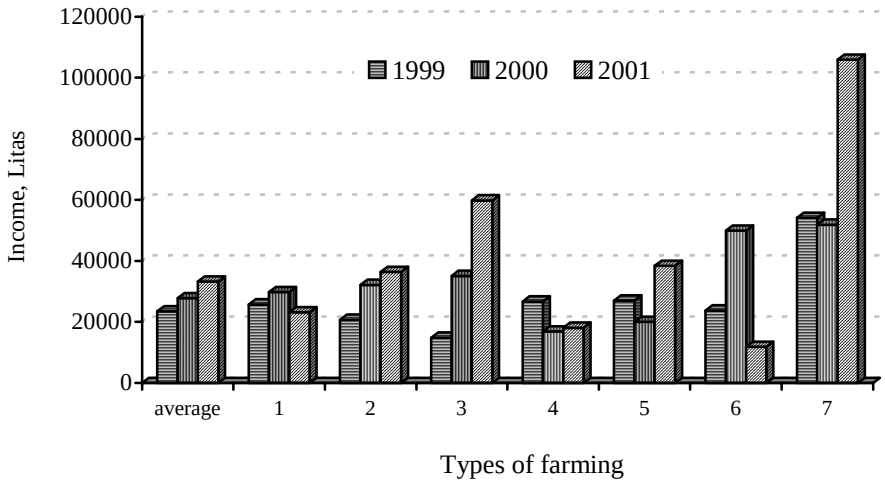
Figure 2. Structure of total output in family farms in 1999-2001



In 2001 income from crop production made up 71% of total income from sales. In the course of 2000 income from sales of other agricultural production increased 2.2 times compared to 1999, however, in 2001 it declined by more than 20% compared to 2000.

In 2001 family farm income was higher by almost 42% compared to 1999.

Figure 3. Changes of family farm income in 1999-2001



1 - specialist cereals, oilseeds;
2 – general field cropping;
3 – cattle-dairying rearing and fattening combined;
4 - mixed cropping;
5 – mixed livestock, mainly grazing livestock;
6 - mixed livestock, mainly granivores;
7 – various crops and livestock, combined.

The largest family farm income was obtained in mixed farms of crops and livestock, combined and cattle – dairying, rearing and fattening combined. In 2001 the share of state support made up 30% of family farm income, while in 2000 – only 12%. Cereal farms were supported most (46%), farms of various crops and livestock, combined – the least (10%).

Figure 4. Share of subsidies in family farm income, in per cent

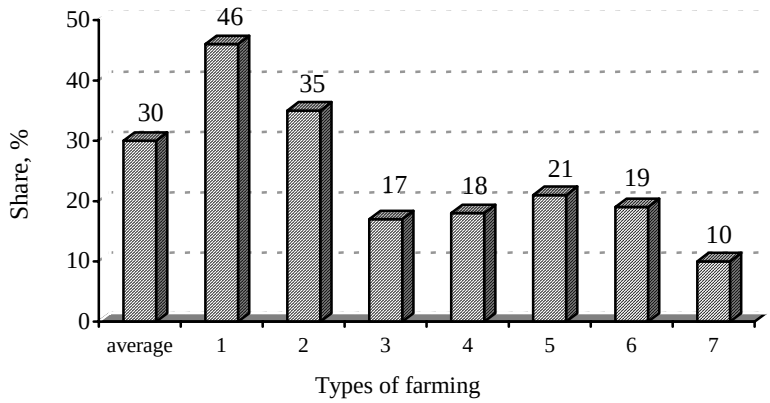
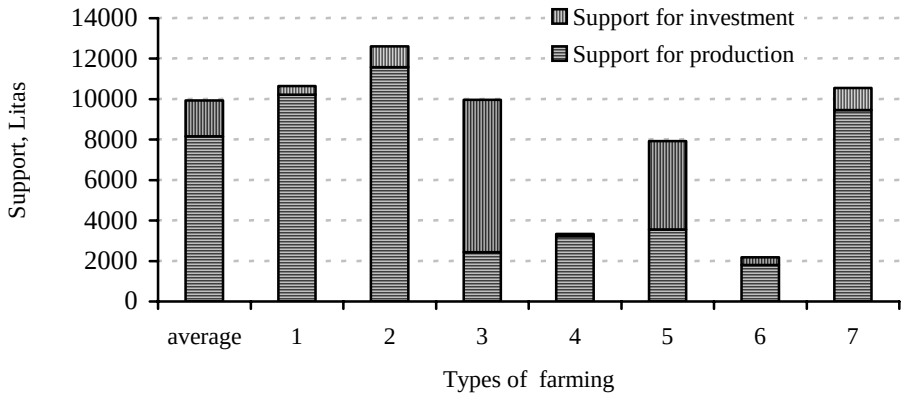


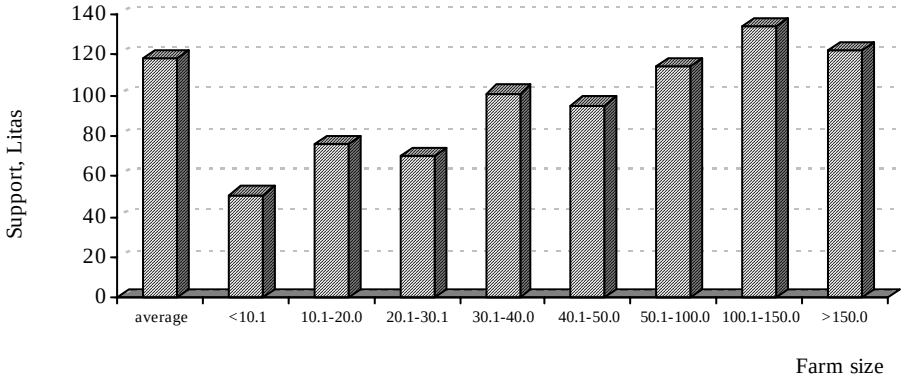
Figure 5. State support for family farm according to types of farming in 2001



In 2001 family farms that cultivated crop production received most support for production, while dairy farms received most support for investments, because the milk sector has a high priority.

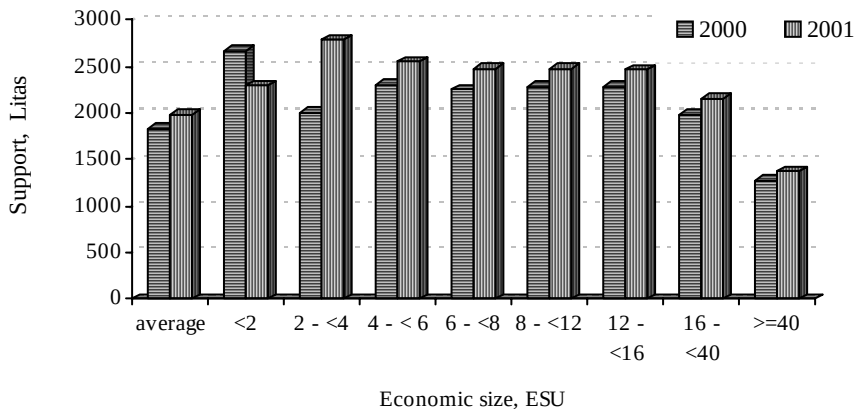
Analysing the state support per 1 ha UAA, a tendency may be observed that the larger the size of a family farm receives the higher support.

Figure 6. State support to a family farm according to farm size, per 1 ha UAA in 2001



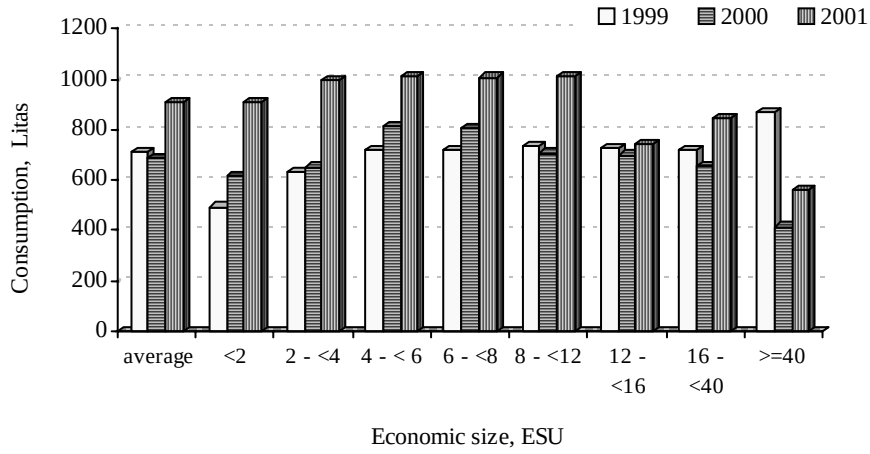
The larger the economic size of a family farm, the higher the family farm income. However, when calculating income per 1 ESU, family farm income goes down in larger family farms. Such a tendency proves once more higher support to crop production.

Figure 7. State support to a family farm per 1 ESU in 2000–2001



In the course of 3 years private consumption of own production per capita increased by 27.5% and reached 907 Litas. In general, consumption of own production makes up a small part of the total output in the survey farms. On the other hand, analysing this indicator with regard to economic size of a farm, a conclusion may be drawn that consumption goes up together with the increase of the economic size up to some limit, and afterwards it declines. Large farms consume less of their own production.

Figure 8. Private consumption of own production per capita in 1999-2001



Labour input permanently declines in family farms, *e.g.* in 2001, on average, 2.67 annual working units were involved in agricultural production. It fell by 4.6% compared to 2000, and by 8.9% compared to 1999. Family labour constantly decreasing, however, hired labour grew. In 2001 Farm Net Value Added per annual working unit reached 14 812 Litas. It was 16% and 90% higher compared to 2000 and 1999 respectively. Farms of mixed cropping endured the smallest changes in the course of the three years, though this indicator was the lowest in farms of this group.

Conclusions:

1. In 2002 about 40 000 farms were registered. In the FADN survey, about 3% of the family farms participated. thus, the number of survey farms is sufficient to make conclusions about farming results in commercial farms. Survey farms produce about 3-4% of total output. The representation of farms will increase after the Agricultural Census in June 2003.

2. State support grew over the course of the period mentioned above, and this influenced family farm income considerably.

3. In 1999–2001 family farms received higher income, which allowed them to better meet their demands using own production and develop their farms.

4. Labour input per family farm participating in the FADN survey declined during the period mentioned above.

Session 1 Discussant Paper

By Mr. Antero Tuominen

Professor Hill has given us an excellent conceptual presentation of farm household income and related concepts, and he has shown how to measure them statistically. Ms. Moreddu has described the situation in Western Europe, or more generally, in OECD countries. Both these papers provide an excellent background when we wish to discuss the situation in the Baltic countries as presented in the three country reports.

However, I would like to begin my comments with a few remarks of a more general nature.

The level and development of agricultural income is generally not the sole objective of the agricultural policies that are in place in our countries. There are or have been also other objectives such as maintaining or reaching a certain level of agricultural production, maintaining a viable agricultural sector over several generations, maintaining rural infrastructure, encouraging structural development of agriculture, etc. The environmental objectives are gaining increasing importance, including sometimes the use of traditional production methods to restore the "natural" state of the environment (*e.g.* the use of grazing when it is not justified economically, etc.).

Sometimes these objectives may even be somewhat in conflict with each other, and their relative weight may change over time. The articles of the Rome Treaty on which the Common Agricultural Policy of the EU is based are clearly a product of the late 1950s. We are dealing with historical processes where time is an important factor. Typically modern agriculture requires long-term investment which creates a capital stock that is rather specific to agriculture and not easily converted to other uses. For these and other similar reasons we cannot design policy from scratch according to rational principles. We do not always have one instrument to achieve one target, but may – for various reasons – have to try to do the impossible: achieve several targets with one instrument, or use some confusing combinations of instruments.

Farm households usually have several sources of income. According to the OECD study agricultural income varies in Europe from one third to two thirds of the total income of farm households. This covers many different situations. What I wish to underline, however, is that all income components of a farm household are important, and it would be wrong to conclude that the income policy aspects of agricultural policies could be forgotten just because they have other important sources of off-farm income. But, it would be equally wrong to adopt the traditional farmers' organisations view according to which only agricultural incomes matter.

In itself there is nothing new in the ideas suggested by the OECD. For example, in my country there were in the 1940s and '50s a very large number of small farms, and it was never suggested that these small farmers would get all of their income from the farm. During the winter the husbands and sons worked in the forestry sector either as paid labourers or as small entrepreneurs, and the total income was sufficient to guarantee a very modest standard of living. The mechanisation of forestry work changed the conditions in the '60s, and with the loss of this part of income, agricultural revenues alone could not guarantee a sufficient standard of living and the farms were no longer viable. At the same time a rapid mechanization of agriculture took place. These developments lead to large migratory flows within the country and even to large-scale emigration.

Attempts to improve the situation of small farmers by increasing agricultural prices and subsidies did not produce the desired results but it slowed down the structural change for a period of time while at the same time creating new problems.

Similarly, if the agricultural part of the income were lost – due to policy changes, developments in the markets or for other reasons, the off-farm income might not be sufficient to guarantee the required minimum standard of living and it might not be possible to increase this part to replace the income lost due to policy changes or market or other development. Employment opportunities may simply not be available.

The country reports presented by the representatives of the three Baltic countries reveal a picture that is rather different from Western Europe. This is particularly true of Latvia and Lithuania. The rural and agricultural incomes seem to be clearly lower than the national average income. Even more importantly, in Latvia the net income from agricultural production for farm households is only a quarter of the total income, and the major part of income comes from social transfers. The situation is somewhat similar in Lithuania; in particular if we look at the cash income of farmers. Even in Estonia social transfers form an important part of the revenues of rural households. These social transfers seem to be above all, although not exclusively, pension payments. The agricultural income seems to be on the increase, but it is low, particularly in comparison with other countries.

If in Western Europe we have a situation where the income of farm households is roughly equal to that of all households, a little more or a little less, in the Baltic States the income of farm households is clearly less than average and the share of agricultural income is smaller. The large share of pension payments and other social transfers seems to indicate that small-scale agriculture is in Latvia and Lithuania compensating the low level of social security payments and acting as a form of social security. Part of the agricultural income is in kind, *i.e.* production for own use, which underlines this trend.

It is hard to see what will happen to this kind of agriculture in the future. The young will probably move to cities because clearly there are too many labour resources tied in agriculture. This is not true of Estonia, however. If it were only a question of old people complementing their small pensions, the problem would be solved by the passing of time. Poverty would be alleviated with economic growth and the possibilities to increase pensions or other social transfers brought about by a higher rate of GDP growth.

For others, with somewhat larger farms the implementation of the Common Agricultural Policy of the European Union will mean annually increasing agricultural income regardless of the possible changes on the CAP that may or may not be decided before the accession of the Baltic States to the European Union.

But this leaves a large group – at least in Lithuania, probably in Latvia but less so in Estonia, whose farms are too small to be viable in the enlarged Union and whose owners are still relatively young or middle-aged. Even they benefit from some aspects of the Common Agricultural Policy but at the same time they may – as small farmers – find it difficult to comply with some EU norms. Milk quality is perhaps an example. These farmers clearly need off-farm income other than just social transfers, but how can this income be generated? In principle the second pillar of the Common Agricultural Policy is there to provide funds for rural development projects, but if the rural environment is not dynamic and entrepreneurial such projects may not spring up, and even more importantly, the necessary off-farm jobs (full-time or part-time) will not be created. If they receive cash payments from the CAP it will increase their income (albeit to a limited extent), but these

payments will do nothing to increase the dynamics. They may even increase the passivity and conserve the existing situation for a longer period.

Is this a problem that is to be solved by agricultural policy measures (by increasing agricultural revenues and restructuring the farms), by social policies (increased transfers when we are dealing with a hidden unemployment problem in rural areas) or by active labour market policies (by training programmes to increase skills and encouraging labour mobility).

It is obvious to me that too many farmers, too small farms and too low productivity are a problem at least in parts of Lithuanian and Latvian agriculture. General economic policy measures and labour market policy measures and social policy measures are required to create an economic and social environment where the problems can be solved. We should not, however, forget the need for agricultural policy measures also. The changes do not take place overnight, but the adjustment will take a long time.

It is interesting to note that although the famous PSE figures are lower for the Baltic States than for the present members of the European Union, all three countries spend almost the same share of their GDP to support their agriculture as the EU does, Estonia somewhat less. Of course in absolute terms the figures are quite different because the GDP per capita is much lower in the Baltic States, but this merely shows how great the effort required is. And noting that the largest single support measure to farmers in Latvia is the rebates on the excise tax on fuel we have to ask ourselves why it is that such a measure is applied when OECD studies show that input subsidies are the least effective way in maintaining farmer's income.

The answer is, of course, that similar measures are in use in many countries of the OECD (agricultural fuel is not taxed). The problem is that small farmers may have a liquidity problem, and lower or subsidized input prices seem a natural solution, which might also be administratively simpler than some other forms of support. At least it is politically easier to introduce, it attacks the same problem that the farmer complains about (high input prices) and once it is introduced it is extremely difficult to replace with an equivalent measure which might be more cost-efficient according to OECD studies.

Accession to the European Union will impose new constraints on the agricultural policies pursued by the Baltic States. They can no longer choose the instruments to be used freely. At the same time it will provide funds to finance the structural development of their agriculture. The increasing emphasis on rural development measures and funds available for these will hopefully help to generate the necessary off-farm income and employment in rural areas. The CAP will guarantee the maintenance of the agricultural share of farm household income, and in the acceding countries this income will increase for the next ten years. Thus, the accession to the EU should also provide new opportunities.

Session 1 Discussant Paper

By Mr. Siemen van Berkum

First of all let me thank the three lead speakers for their excellent exposition of developments and trends in rural income and employment in the Baltic countries.

The three country papers provide a comprehensive overview of the past and present income levels and structure in the rural areas of the three Baltic countries. The story is not cheerful. All three papers indicate that income in rural areas is below the national average level, that income from agriculture is below the average income level in the rural areas, that income from agricultural activities decreases and that unemployment in rural areas increases. The income and employment situation in rural areas looks bad and the picture for agriculture is even worse. The livelihood of many people living in the rural areas of the Baltics seems to be seriously under pressure. This observation makes the discussion of the issues of this seminar very topical.

In this short contribution I would like to make two observations, which I will comment on and I will try to indicate ways to improve rural incomes.

Rural incomes are always below income levels in urban areas

All three country papers indicate that rural income levels are below urban income levels. The phenomenon of income disparities between urban and rural regions is widespread: for example, figures for the EU show that income levels in rural regions are on average 20% below the national average and 30% less than income levels in most urban regions (Table 1). Rural-urban income disparities have a structural character: the situation in the EU did not change over the period 1980-1993. The reasons behind this regional income disparity are purely economic. Firstly, as highly educated people and well-paid jobs are concentrated in urban regions, the highest income levels are in urban regions. Secondly, absolute income levels in rural regions may be lower than in urban regions, but costs of living (housing, food) are lower too. This implies that the purchasing power of 1 euro earned and spent in rural regions is higher than the same euro in urban regions. Therefore, relatively low productive labour is located in rural regions as it may earn enough for a reasonable living in the rural regions. The consequence of both arguments is that rural income will never be on the same level as urban income. This situation is not an imperfection that needs to be dealt with through government intervention, but the result of proper labour market functioning.

Table 1. GDP per capita in the EU, 1980-1993 (index EU average = 100)

Year = 1980				Year = 1993			
Most rural regions	Intermediate rural regions	Most urban regions	EU Average	Most rural regions	Intermediate rural regions	Most urban regions	EU Average
79	96	110	100	80	97	109	100

Source: Terluin, I.J., Rural regions in the EU: Exploring differences in economic development, NGS, Groningen, 2001, p. 31.

Low income levels in rural areas are related to underdevelopment of the agricultural sector

The relatively low income levels in rural areas are connected with a poorly developed agriculture, as illustrated by a large share of the total labour force employed in agriculture. In the Baltic countries, agricultural employment is especially important in Lithuania with a share in total employment of 20%. However, these 20% of the labour force earn only 7% of the total Gross Value Added (GVA),

implying a very low labour productivity in the agricultural sector. In Latvia the agricultural labour force is 14% of the total labour force and earns only 4% of GVA. Estonia has a relatively small agricultural labour force, yet almost double the present figure of the EU-15 (Table 2). For comparison: in the 1950s the share of agricultural employment in total employment in the Netherlands was in a similar range of percentages as in Lithuania and Latvia now. Since then, however, agricultural employment in the Netherlands decreased and labour productivity increased rapidly due to modernisation and restructuring of the sector.

Table 2. Agricultural employment and GVA (%, 2000)

	Share of agricultural employment in total employment	Share of agricultural GVA in total GVA
Lithuania	20	7
Latvia	14	4
Estonia	8	5
EU-15	4	2

Source: EU Commission, Agricultural Situation in the Candidate Countries – Country Reports, 2002.

How to improve rural incomes?

In principle there are two ways to improve rural incomes:

a. Adjustment of the agricultural structure.

b. Creation of non-agricultural employment.

In the Baltic countries the problem of low income and high unemployment in rural areas is to a great extent a problem of the agricultural sector, as a significant share of the labour force is employed in or dependent on agriculture. Agriculture is therefore a major economic activity in rural areas in the Baltic countries. Prosperity in rural areas is thus very sensitive to changes in the profitability of agricultural activities. It seems, therefore, logical that a solution for socio-economic problems in rural areas lies in the strengthening of the agricultural sector.

The agricultural sector can be strengthened through agricultural structural policy, like measures such as investments in modernisation of agricultural farms, investment in research, extension and education, in land consolidation and in infrastructure. With the latter I mean besides investment in physical infrastructure like roads or auctions also investment in legal infrastructure, for instance, in the field of contracts (enforcement) and co-operation forms. The instruments mentioned are under the heading of the present rural policy of the EU. The accession countries can apply these instruments in the framework of SAPARD, in which the EU provides co-finance support.

Policy aimed at modernising the agricultural sector in order to strengthen the competitiveness of the sector will lead to an increase in scale of farms and labour shedding. This process will create a large social problem in the Baltics (and in other accession countries where the same process takes place), if there is no alternative employment in the rest of the economy for this surplus labour from the agricultural sector. Therefore, regional or industrial policy has to focus on the creation of non-agricultural employment (industry and services).

Agricultural structural policy should go hand in hand with industrialisation and regional policy in order to create non-agricultural jobs. Such policies have been applied in West-European countries in the first decades after World War II. For instance, agricultural development in the Netherlands in the

1950s has been stimulated by policy initiatives to encourage industrialisation. A wide array of measures were applied, such as public investment in infrastructure like roads and business sites, investment incentives like tax exemptions, loan guarantee funds for small and medium businesses, vocational and other training facilities, etc. These measures were rather successful in terms of employment creation outside agriculture, although it is difficult to indicate the effectiveness of the policies, as the economic situation in the Netherlands was very favourable in the 1960s. The Latvian paper mentions that the government has recently implemented several credit programmes, among others for non-agricultural business development. Such programmes, complemented by adequate action for the development of infrastructure and human resources will encourage the creation of non-agricultural employment and are therefore a promising road to the improvement of rural incomes in the Baltic countries.

SESSION 2. DEVELOPMENTS IN THE LABOUR MARKET AND FACTORS AFFECTING LABOUR MOBILITY IN RURAL AREAS

A FRAMEWORK FOR ANALYSING LABOUR MOBILITY IN AGRICULTURE AND RURAL AREAS OF TRANSITION COUNTRIES

By Dr. Johan F.M. Swinnen and Ms. Liesbeth Dries
(Paper presented by Dr. J.F.M. Swinnen)

Abstract

A large share of the population in Central and Eastern Europe (CEE) lives in rural areas. The share of agriculture in total employment varies from around 5% in high income countries to more than 40% in poorer countries. Transition has had a dramatic effect on agricultural and rural employment. In some countries agricultural employment has fallen to one-third of the pre-reform level. In this paper we present a framework for analysing labour mobility and employment changes in rural areas of transition countries. We identify a series of key factors and discuss possible implications of EU accession.

Introduction

A large share of the population in Central and Eastern Europe (CEE) lives in rural areas. The share of agriculture in total employment varies from around 5% in countries with the highest income per capita, such as Slovenia and the Czech Republic, to more than 40% in Romania and Albania. In the Baltic countries agricultural employment ranges from 7% of total employment in Estonia to almost 20% in Lithuania.

Transition has had a dramatic effect on agricultural and rural employment (Table 1): in some countries agricultural employment has fallen to only one-third of the pre-reform level (Figure 1).[1] What is also remarkable is that rural labour adjustments have differed strongly between countries.[2] During the first years of transition, labour employment in agriculture declined dramatically (around 50%) in countries such as the Czech Republic, Slovakia, and Hungary. In contrast, agricultural employment fell only moderately in Poland and Slovenia (around 15-20%), while it increased in, for

1. Data on employment and labour use should be interpreted with care, since there are important statistical problems with the data. To the extent possible we have used the most reliable data in this paper; but even these should be interpreted with care. First, statistical information may hide the fact that many people registered as "employed in agriculture" are working part-time in other sectors. For example, according to 1998 estimates of the Institute of Rural Development and Agriculture, 60% of inhabitants of rural areas in Poland were "connected to a farm", but for only 20% of them it was their main occupation, and for only 10% their only source of income (Sztanderska and Piotrowski, 1999). Second, changes over time may reflect changes in definitions or interpretations. For example, in the Czech Republic, the number of farm workers declined from 533 000 (of which 150 000 in non-agricultural activities) in 1989 to 201 000 (of which 30 000 in non-agricultural activities) in 1997. The decline in farm workers includes 120 000 (approximately 30%) due to separation of non-agricultural activities from farms, which could be thought of as mostly a "statistical effect".

2. These diverging evolutions are especially remarkable because other input adjustments have been relatively common across transition countries. For example, land use has decreased only slightly over the first decade of transition (-5% on average), capital use declined somewhat more (for example, tractor use declined on average by 15%) and fertilizer use collapsed (-80% on average) (Rozelle and Swinnen, 2003).

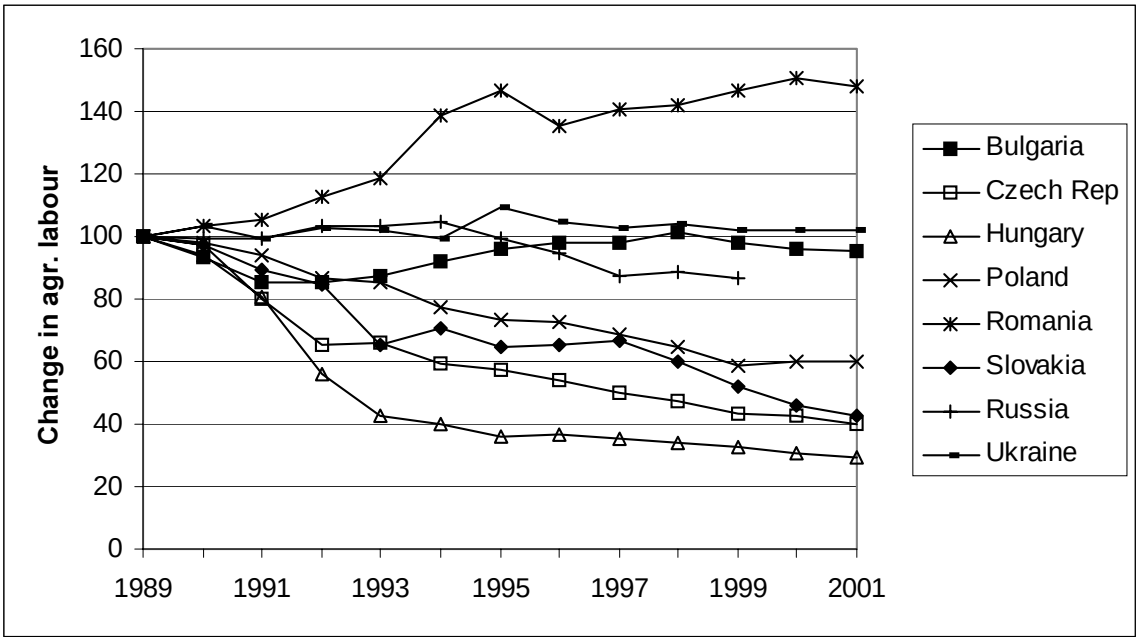
example, Romania and Russia. Also in the Baltic countries, labour changes differ. Figure 2 illustrates how agricultural employment declined by around 60% during the first five years of transition in Estonia, while the changes were much smaller in Latvia and Lithuania. In these countries, important declines in agricultural employment occurred only after 1996.

Table 1. Average annual change in employment in CEEC agriculture (%)

	1989-1993	1993-1997	1997-2001
Bulgaria	-3.2	3.0	-0.8
Czech Republic	-9.4	-6.7	-5.6
Estonia	-10.4	-14.6	-6.9
Hungary	-18.7	-4.6	-4.5
Latvia	2.5	-2.1	-8.0
Lithuania	2.9	-2.3	-10.0
Slovakia	-9.7	0.6	-10.3
Slovenia	-2.5	5.2	-4.1
CEEC-8	-6.1	-2.7	-6.3
Poland	-3.9	-5.2	-3.2
Romania	4.4	4.8	1.3
CEEC-10	-4.8	-2.2	-5.2

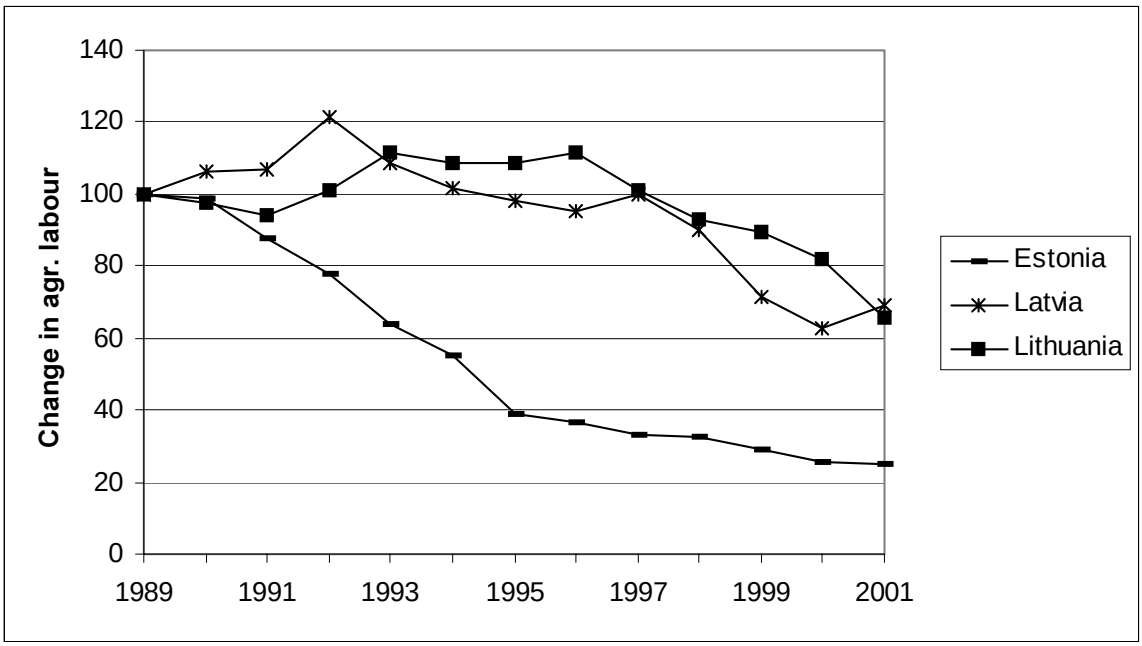
Source: Own calculations based on ILO, OECD, and National Statistics.

Figure 1. Change in agricultural employment in CEECs



Source: Own calculations based on data from ILO, OECD, and National Statistics.

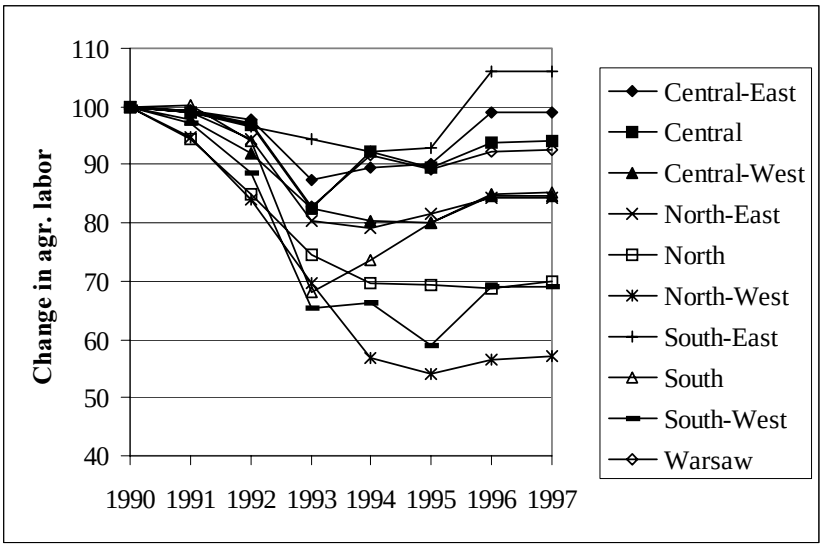
Figure 2. Change in agricultural employment in the Baltics



Source: Own calculations based on data from ILO and National Statistics.

Not only do we find different adjustments between countries, but also *within* countries. Figure 3 illustrates how the average adjustment indicator for Poland hides important regional differences in labour adjustment. Labour outflow was strong in the northern and north-western regions, while much less in the eastern and southern regions.

Figure 3. Change in agricultural employment in Polish macro-regions (*)



Source: Own calculations based on GUS.
(*) Series cannot be updated after 1997 because of a disruption in the statistics with the reorganization of the regions in Poland.

These observations obviously raise the issue of: Why? What are the reasons for these differences in labour adjustments? And, what do they imply for future adjustments and labour market policies?

The literature points at two arguments, which would induce major adjustments in agriculture. A first group of studies point at pre-transition distortions and argues that, while labour in most sectors of the economy was inefficiently employed, this was especially the case in agriculture.[3] These studies implied that liberalisation would induce a shift to a more efficient distribution of labour in the economy and would thus cause an outflow of labour from agriculture to other sectors. A second group of studies focus more on the transition process itself and argues that the agricultural sector has played a buffer role during transition: absorbing labour laid off in other sectors, and as a source of income and social security during the difficult transition time period.[4] The remarkable thing is, when comparing these predictions with the actual developments in Figures 1 to 3, both arguments seem to have been right – or neither, depending on the way one looks at it.

In the rest of this paper we present a framework for analysing labour mobility and employment changes in the rural areas of transition countries. We identify a series of key factors and discuss possible implications of EU accession.

Conceptual framework

There is an extensive literature and a variety of models on the determinants of agricultural employment and rural migration.[5] These are important in order to understand employment developments in transition agriculture and rural areas, but not sufficient. The specifics of transition from communist to market based agriculture require additional features to be explicitly integrated in the modelling. To explain this, we proceed in three steps.

First, a useful conceptual approach is to focus on the *decision-making process of individuals* who are employed in agriculture, and who weigh the costs and benefits of leaving agricultural employment for other employment, either in rural or urban areas. Their decision will be affected by several factors. These factors include:

- The relative income obtained in agricultural employment compared to other employment. If income is higher in other sectors, people will have an incentive to move to other jobs. However the income which is relevant is not necessary current income, but rather the total of current and discounted future income streams over the period of employment. (Notice that this can also refer to unemployment benefits: if these are high enough compared to other income, people may prefer unemployment.)

- Other benefits associated with employment in specific sectors. Some people may prefer working in agriculture because of non-pecuniary benefits, *e.g.* cultural reasons, because they prefer "being their own boss" rather than working in a company, etc. Alternatively, better social conditions and less income risk in other jobs may be attractive features of employment outside farming.

- The probability of finding employment: even if incomes are higher in a specific sector it may not matter much unless one gets a job in the sector.

3. Brada (1989), Jackman (1994).

4. Seeth *et al.* (1998), Leiprecht (1999).

5. See *e.g.* Taylor and Martin (2002) for an overview.

- The costs of moving from one job to the next. These costs can include costs of searching for other employment, costs of migration to other areas, etc.

Second, it is important to integrate the employment choices by individuals in a *household decision-making process*.[6] As with assets, households can allocate labour to more than one activity, and in doing so reduce risk by diversifying income sources; or access financial sources it may require in farming, which it cannot get through other financial institutions.

These considerations are important in general, as is demonstrated by the importance of *e.g.* part-time farming in Western market economies. They are particularly important in transition economies where rural credit markets function very imperfectly, if at all. Accessing inputs and output markets are also an important reason why rural households may allocate part of their labour to individual farming, while keeping some of their assets and labour in co-operative farms. By doing so, it helps them access inputs and output markets through the large scale farm organisations.

Notice that such household labour allocation decisions may even imply sending household members abroad if the incentives are strong enough. The most extreme case of this is in Albania, where income from remittances is the most important source of income for most rural households, and an important source of rural credit (Germenji, Sarris, and Swinnen, 2003).

A related issue is human and social capital. It is clear from empirical evidence that not all individuals are equally likely to move to different jobs under similar conditions. Household members with specific skills and characteristics are more likely to find alternative employment, or are more likely to move to different jobs. Social capital affects employment changes in a variety of ways. It may reduce information costs in alternative employment searches or reduce transaction costs in job mobility when this implies moving to different regions, finding housing, etc.

Third, what is very different from Western market economies is the *farm structure and restructuring process* in transition countries. With the exception of Poland and former Yugoslavia, agricultural employment was concentrated in large collective and state farms. A conceptual model of agricultural and rural employment can not be satisfactory unless it explicitly integrates these structural aspects in the analysis. In order to understand how this restructuring process affects employment, one needs to separate "restructuring" into several parts:[7]

- The introduction of hard budget constraints caused a reduction in farm employment, as farms cut back "overemployment".

- Improved management with farm reorganization caused an increase in farm employment as labour became more productive.

- Individualization of farming caused several effects, including (ceteris paribus):

  – Extra employment due to workers influence on management is reduced.

  – More efficient use of labour, which directly caused an increase in labour demand.

6. See Rizov and Swinnen (2002) for a formal model.

7. We summarize here key results, and refer to Dries and Swinnen (2002) for a formal presentation of the model and derivation of the results.

– And which indirectly reinforced more labour demand as more efficient labour substitutes for other inputs.

– Under transition conditions, losses of scale efficiency can be considerable, in particular when rural credit markets function imperfectly. As a consequence, labour demand decreases with losses in efficiency, but at the same time increases due to the substitution effects, as labour substitutes for missing capital inputs.

– As agricultural employment shifts from formal farm employment to more informal household-based farming, officially recorded employment may decrease.

The net effect of individualization of farming cannot be derived from the conceptual model, since several of the sub-effects go in opposite directions. However, in our empirical studies we find that the net effect of a shift to household and family farms is higher agricultural employment, ceteris paribus.

Clearly, each of the factors discussed here in this conceptual framework is influenced by a set of environmental, economic, institutional, and household-specific characteristics. We will discuss the impact of some key characteristics here and provide some empirical evidence to illustrate their impact.

Factors affecting employment in rural areas of transition countries

Agricultural support policies

Price policy and farm subsidies affect agricultural employment through their impact on relative income. At the start of transition, price liberalisation and subsidy cuts had an important negative effect on demand for labour in agriculture in all CEECs.

This reduction in demand was offset by an increase in labour demand as price liberalization also changed the relative factor costs. In particular, prices for other inputs (especially capital inputs) increased relative to wages. The latter caused a substitution of labour for other inputs and contributed to the increase in agricultural employment during transition.

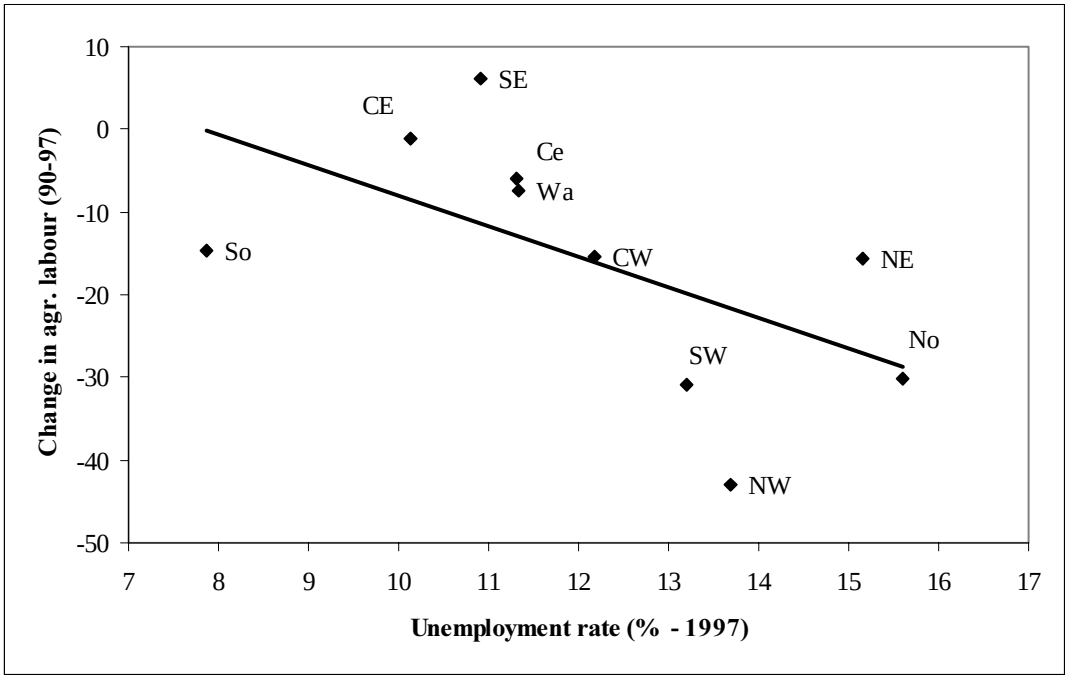
However, the impact of price policies and farm subsidies depends strongly on the form of the policies. OECD estimates show that traditional market and price support implies important transfer losses and that the increase in net farm income is relatively small. Studies such as that of Gardner (2000) show that the long run impact of US farm policies on agricultural employment is very limited.

Off-farm employment

Employment opportunities in other sectors are obviously an important factor. When there is high unemployment, people are unlikely to leave agriculture, even when farm incomes are low. However, empirical evidence shows that the relationship between off-farm employment and rural labour mobility is weak. For example, in Poland the reallocation of agricultural labour to the rest of the economy reacted only slowly, at best, to improvements in the general economy. Since 1992 the general economy was characterised by strong growth (average of 5.2 % annually between 1992 and 1998), and, with two years delay, by an impressive decline in unemployment: from 14.4% in 1994 to 10.6% in 1998. Yet there was little effect on agricultural labour, despite low or negative growth in agriculture. After 1998, unemployment has been rising again in Poland (16.1% in 2000), although GDP continued to grow.

The weak relationship between agricultural employment and general unemployment is confirmed by looking at regional developments. When one compares the regional outflows with regional unemployment rates, it is clear that the highest outflow of agricultural labour has occurred in regions with higher unemployment rates (Figure 4). Hence, it seems that labour is not moving out of the agricultural sector as a reaction to better employment opportunities in other sectors.

Figure 4. Agricultural labour adjustment and regional unemployment in Poland (*)



Source: Dries and Swinnen (2002).
(*) Series cannot be updated after 1997 because of a disruption in the statistics with the reorganization of the regions in Poland.

The obvious question is: why not? What is constraining this reallocation of rural labour, important for rural development, and for labour productivity growth and restructuring of agriculture? There are several reasons for this. One has to do with the farm restructuring process; another with the characteristics of the rural labour force, and yet another, with mobility costs between jobs.

Rural market imperfections and constraints

The study by Gardner (2000) shows how the integration of the rural economy in the general economy, in particular concerning the integration of labour and capital markets, is a key factor contributing to income growth in agriculture. Integration of rural factor markets in the general economy and reduction of factor market imperfections have several effects on employment.

On the one hand it increases incomes in agriculture, and therefore demand for labour. A key factor is improved access to capital. *Rural credit and access to finance* is an important constraint, both for farm restructuring and the creation of non-farm rural employment. Rural financial services are underdeveloped. The Business Environment and Enterprise Performance Survey conducted by the EBRD in 2002 shows that rural firms face severe obstacles in obtaining finance, especially long term credit, as a result of collateral requirements, high interest rates and shortage of bank funds (EBRD,

2002). Similarly, farm surveys conducted in Central and Eastern Europe in 1999 identify shortages of capital and unavailability of rural credit as major reasons for the lack of farm development. Even in relatively well-advanced countries such as the Czech Republic and Slovakia, only 9.4% and 4.6% respectively of farmers receive loans from a bank or credit institution.

Integration of rural factor markets in the economy also facilitates the outflow of labour by the stimulation of off-farm rural activities, and by reducing *labour market constraints*, and hence mobility costs for people to move to other sectors and regions. In transition countries, we find that general reforms and liberalisation, which reduced intersectoral mobility costs, had an important impact on labour adjustments in transition countries. In the Czech Republic, Slovakia, Hungary, Poland and Slovenia strong(er) liberalisation of the economy reduced constraints for intersectoral labour mobility. In contrast, overall liberalisation in Romania, Bulgaria, Ukraine and Russia moved much slower, constraining intersectoral labour flows.

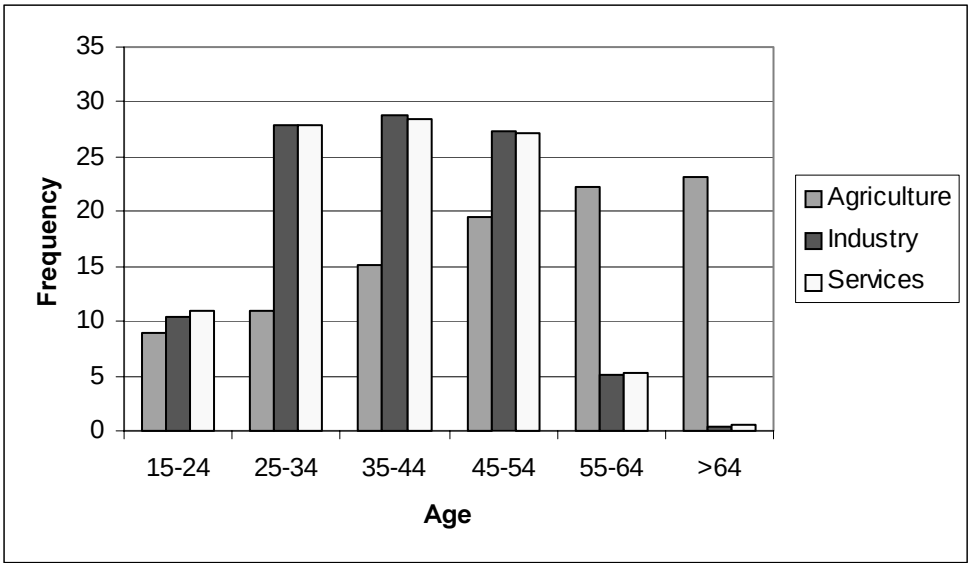
Spatial considerations are important here. In countries where the rural areas were mainly organized around collective and state farms and where non-farm employment opportunities are concentrated in cities, finding off-farm employment may imply moving geographically for households. In other countries, where off-farm employment is closer to farms and available in rural areas, job reallocation may be possible without moving houses. It is clear that these differences strongly affect mobility costs, and hence, household decisions.

Studies show that the lack of housing in urban areas or other factors, such as barter on farms, are important constraints on rural labour mobility. (This is even distinct from formal policy constraints on labour mobility as existed in rural China for a long time.)

Human capital

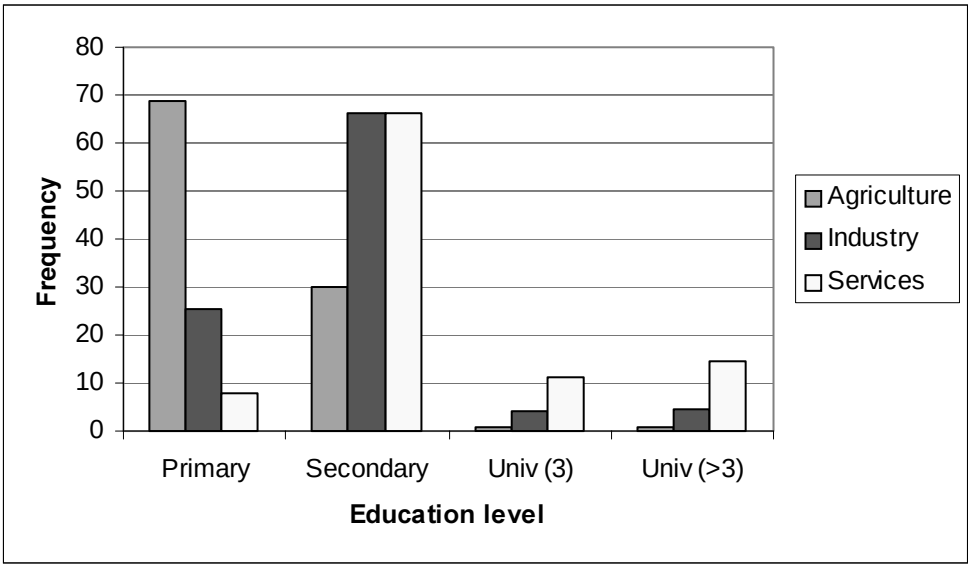
Important constraints on labour reallocation are the structural characteristics of the labour force. As much as 43% of agricultural employees in Poland have only elementary and lower education (compared to 16% in construction, 13% in industry and 8% in services) and 33% basic vocational education. A study by Leiprecht (1999), using labour survey data, finds a strong relationship between the level of education and the likelihood of finding another job in the service sector or in industry. In particular, those with the lowest level of education are handicapped in their attempts to find alternative jobs. We find the same unfavourable labour characteristics elsewhere. In Slovenia, about 45% of agricultural labour is over 55 years old (Figure 5). Similarly, the sector is disadvantaged by a low educated labour force as almost 70% of agricultural labour has, at best, finished primary school (Figure 6). Interestingly, in some of the countries where major labour outflows took place, the agricultural labour force seems less disadvantaged. For example, only 19% of agricultural employment in Estonia is 55 years or older, compared to 13% of the workforce in construction (Figure 7). Also with respect to the level of education, the intersectoral differences are small in Estonia (Figure 8).

Figure 5. Sectoral age distribution in Slovenia, 1999



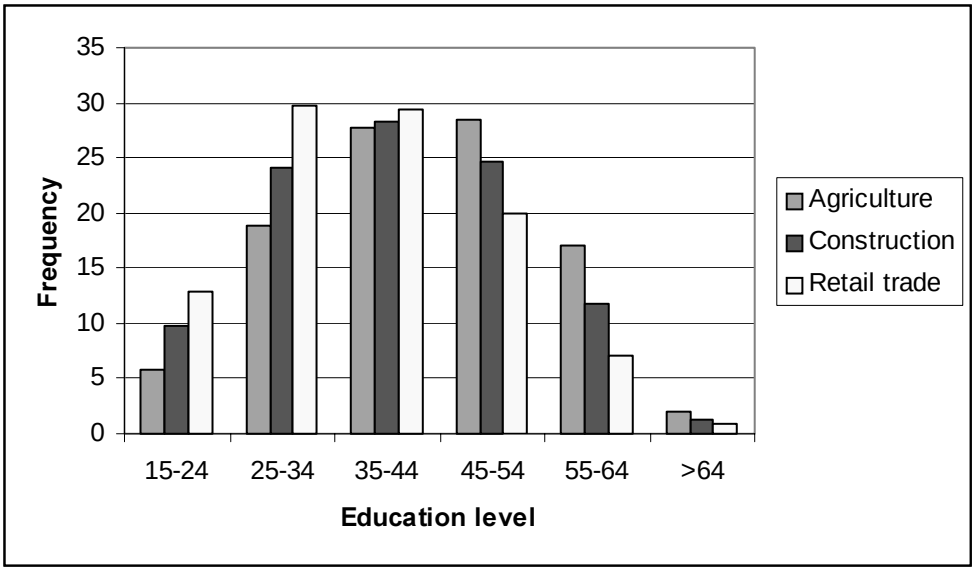
Source: Slovenian Labour Force Surveys.

Figure 6. Sectoral education levels in Slovenia, 1999



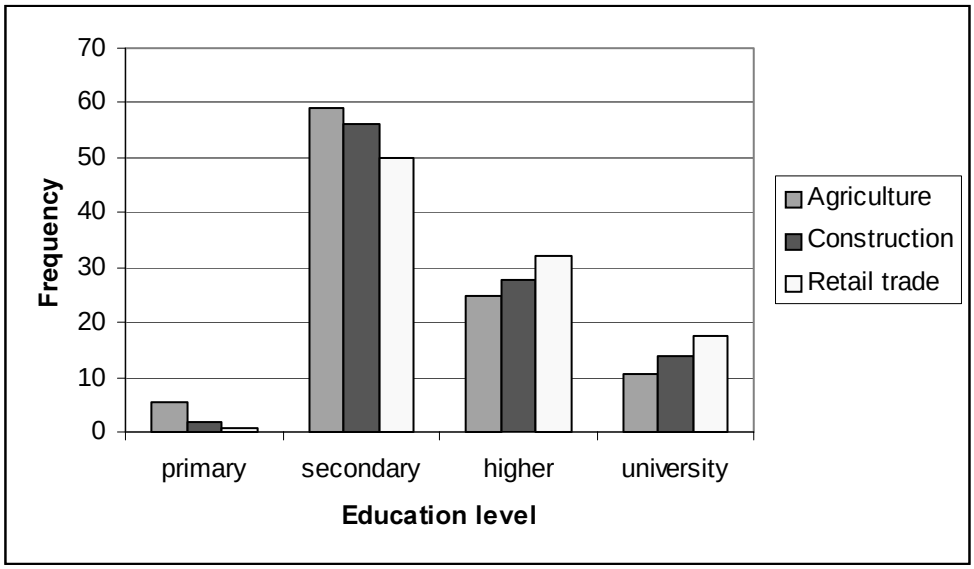
Source: Slovenian Labour Force Surveys.

Figure 7. Sectoral age distribution in Estonia, 2000



Source: National Statistics.

Figure 8. Sectoral education levels in Estonia, 2000



Source: National Statistics.

Inadequate human capital is a very important constraint, not only for agricultural labour restructuring, but more generally for business development and economic activities in rural areas. Empirical studies confirm that in transition countries education is positively correlated with enterprise development, both farming and non-farming. Better education increases the probability of a business start-up and efficiency of the enterprise. Studies find a non-linear relationship between human capital and farming activities. For example, the impact of education on the development of new farming

enterprises is non-linear because beyond a certain level of education individuals tend to leave agriculture and choose non-agricultural employment (Rizov and Swinnen, 2002).

Yet, the factors mentioned above cannot fully explain the major variations in regional adjustment patterns, since they are not regional effects.

Farm restructuring

The reorganization of farms strongly affected labour adjustment. The outflow of labour is strongest in countries such as the Czech Republic, Slovakia, Estonia and Hungary, where large-scale farms have remained important in agriculture. The shift to individual farms is much stronger in transition countries such as Romania, countries which experienced an inflow or preservation of the labour force in agriculture. The break-up of the collective and state farms in labour-intensive agricultural production systems in these countries induced strong gains in labour efficiency.[8] These efficiency gains have reduced the outflow of labour from agriculture.

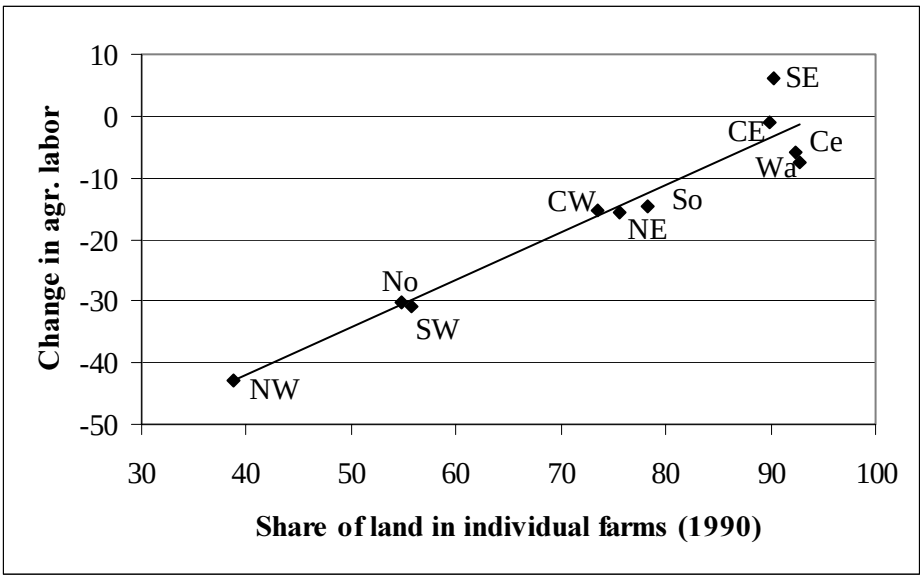
In contrast, reformed collective and state farms with independent company management have laid off a large number of workers, beyond those that voluntarily left the farms for other employment.[9] Moreover, the difference between the Czech Republic, Slovakia and Hungary versus Poland and Slovenia can be attributed to this factor. Both Poland and Slovenia are characterised by a domination of small family farms, even pre-reform. These structures have reduced the outflow of labour.

The importance of this factor is illustrated in Figure 9 which shows for Poland that there is a strong correlation between the regional outflow of labour from agriculture and the importance of state farms in the region at the outset of the reforms. In other words, family labour on small private farms has mostly stayed in agriculture, while many workers employed on the large state farms have been laid-off in the process of privatisation and transformation of these state farms.

8. See *e.g.* Macours and Swinnen (2000).

9. This development is also related to the privatisation process and the land and asset ownership distribution. In transformed collective farms where workers were also members owning land (or other assets) it was more complicated laying surplus workers off than in transformed state farms where workers did not own assets and managers could lay them off more easily.

Figure 9. Initial farm structure and change in agricultural employment (1990-1997) at the regional level in Poland (*)

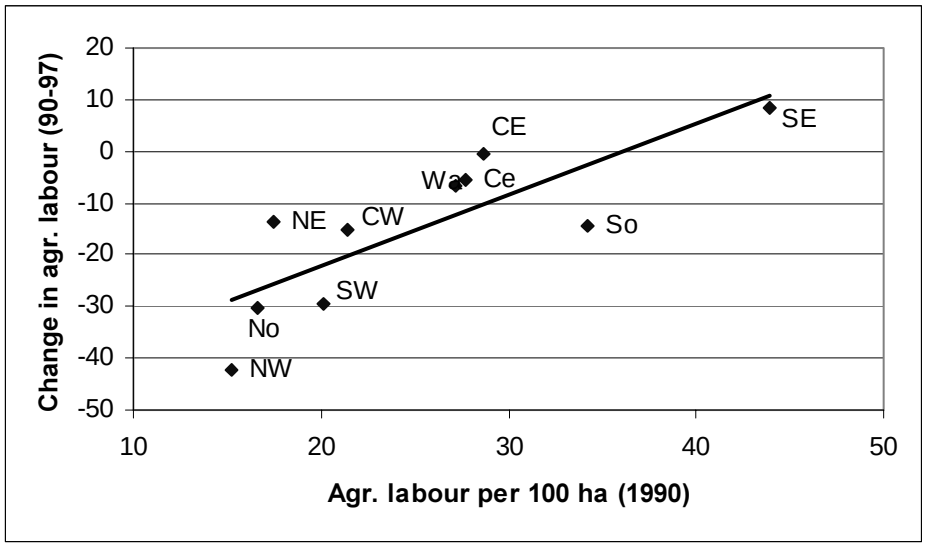


Source: Dries and Swinnen (2002).
(*) Series cannot be updated after 1997 because of a disruption in the statistics with the reorganization of the regions in Poland.

The increase in agricultural employment in some regions (such as the South-East) is due to workers being laid-off in other sectors, such as heavy industry, returning to small farms with which they have a family-connection. Hence, the statement that agriculture is playing a "buffer role" in Poland is only valid for the small family farms and does not apply to the transformed state farms.

What is remarkable is that, as a consequence of this process, labour intensity in farming is not converging across different regions in Poland – and probably different farming regions across Eastern Europe, but instead diverging. This evolution is clear from Figure 10. Labour use has fallen significantly in those regions, where labour intensity was lower at the start of transition.

Figure 10. Diverging patterns of agricultural labour intensity in Poland (*)



Source: Dries and Swinnen (2002).
(*) Series cannot be updated after 1997 because of a disruption in the statistics with the reorganization of the regions in Poland.

Many of the farm workers which were laid-off were not able to find alternative employment in the first years of transition. The importance of the "push factor" (former state farm worker lay-offs) in determining labour adjustments in Polish rural areas is consistent with the fact that, with the exception of the South, most labour outflows occurred in regions where unemployment rates are higher, than in regions with lower unemployment (see Figure 9).

This raises an interesting question then, why workers formerly employed on state farms stayed unemployed rather than taking up self-employment as individual farmers, as was the case with workers laid-off in industries who returned to farming in the south-eastern regions, or with labour who stayed “under-employed” on the family farms. The reason probably has to do with capital in various forms: human capital, social capital, and access to financial and physical capital. Former state farm workers may lack both the practical and managerial experience (specialised tasks in state farms) to start up individual farms. Furthermore, physical capital (land and machinery), needed for the exploitation of a farm needs either to be leased or bought. The uncertainty of future returns due to the relative price shocks and the investments necessary for the start-up of a farm may make the difference between unemployment benefits and expected agricultural earnings, smaller than in the case, where you already have a farm and thus no supplemental investments are needed. Having a farm in the family thus substantially reduces costs for taking up or continuing farming and decreases the probability of agricultural labour outflow to unemployment. Social capital plays a role as industrial labour returning to agriculture was mostly connected with family farms and therefore had easier access to capital and land needed for farming.

This is consistent with observations from Romania, where more new farms were started in regions that already had a tradition of private farming before 1989, that is, where institutions and a culture conducive to private farming were already in place. Further, better access to physical infrastructure, such as roads, transportation facilities, etc. is correlated with more enterprise start-ups in Romanian agriculture (Rizov *et al.*, 2001).

Food and social security

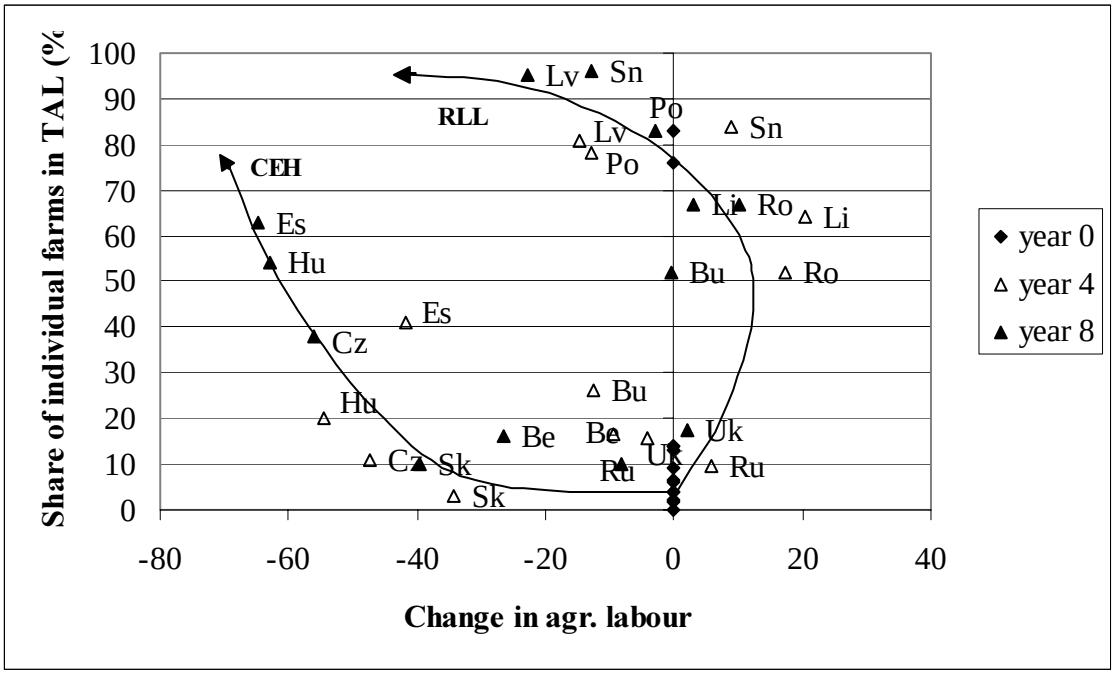
Food security or, more generally, social security considerations played an important role in household strategies regarding labour allocation to farming. In low income transition countries, household farming provides food and social security. This household security strategy limits the outflow of labour from agriculture in the poorer countries and coincides with the growth of individual and household farms.

This is in contrast to higher income countries such as the Czech Republic, Slovakia, and Hungary, where the state provides more extensive social security and unemployment benefits, pensions etc. For example, in the Czech Republic and Slovakia, about half of all farm workers retired (OECD, 1999).

Patterns of labour adjustment

The combination of these factors has contributed to different patterns of transition in the labour market. To illustrate the dynamics of labour adjustments and the differences among countries, Figure 11 presents the various countries positioned in a two-dimensional labour-farm restructuring framework. Among the countries that start from similar initial conditions (*i.e.* less than 10% of land used by individual farms at the outset of the reforms (this excludes Poland and Slovenia)), we can identify clearly distinct patterns.

Figure 11. The Dynamics of Labour Reallocation and Farm Restructuring in Transition



[a] Start of the reforms in CEEC = 1989, in FSU = 1990; 8 years after reforms is 1997 for CEEC, except Slovenia (1996), and 1998 for FSU.
Source: Swinnen *et al.* (2003).

One pattern includes the Czech Republic, Estonia, and Hungary (CEH). In these countries transition has first induced massive agricultural labour shedding, while many of the large-scale

corporate farms continued to dominate agriculture. At the start of transition (year 0) the CEH countries had an average of 10% of land used by individual farms. After four years of transition, on average, agricultural employment had fallen by almost 50%, while corporate farms continued to use 75% of land. Only in the second transition phase (year 4-8) there is a significant shift to individual farms: more than 50% of the land is now used by individual farms, while labour shedding continues, but at a slower rate.

A different path was followed by countries such as Romania, Lithuania, and Latvia (RLL). In these countries, which started from the same position as the CEH group, there is an immediate and dramatic shift to individual farms, while labour use increases, on average, in agriculture. After 4 years, individual farms use 65% of the land and labour use has increased by 8%, on average. In the second transition phase, the shift to individual farming continues to increase, albeit slower, and there is a turnaround in labour use: employment in agriculture falls in all countries (on average by 10%).[10]

These differences in adjustment paths are due to a combination of initial conditions and reform policies. In terms of initial conditions, CEH has a higher level of development than RLL (reflected in higher income and lower share of agriculture in employment). The lower level of development and income makes it more likely that farm workers will shift to individual farms for food and social security reasons. This process is reinforced by higher labour intensity in RLL, which stimulates a shift to individual farms because it both reduces the disruption costs and potential scale diseconomies of farm restructuring and increases the benefits of shifting to an organisation with better labour management. Furthermore, government regulations have been more conducive to the move to individual farms in RLL than in CEH. For example, in Latvia there was a strong government policy directed at breaking up the collective farms, which were seen as bastions of communism (Rabinowicz, 1997), while in Romania the shift to individual farms occurred partly spontaneously with collective farm members breaking up the collective farms and forcing governments to follow with regulation. In combination, these factors caused a shift to individual farming have also contributed to a slower reduction in agricultural employment in RLL compared to CEH. In the latter group, reformed corporate farms have laid off many workers.

These different adjustment procedures have been reinforced by two other differences. First, the relative decline in labour costs vis-à-vis other inputs was - 65% in RLL compared to only - 26% in CEH, providing much stronger incentives for input substitution through labour in RLL. Second, the considerably stronger progress in liberalization of the overall economy in CEH reduced mobility costs to other sectors more than in RLL.

CEEC labour adjustments and EU accession

A key factor in future employment developments in CEEC rural areas is the impact of EU accession. EU accession will have several effects on rural employment. Accession may slow down the shedding of labour from agriculture because of the inflow of CAP subsidies. On the other hand, further employment reduction in agriculture will result from the need to restructure and increase productivity in agriculture, as well as the increase in job opportunities in the rest of the economy with growth in other sectors. The latter is expected to be reinforced with enlargement.

Similarly, the availability of additional government funds for structural and rural development policies through *e.g.* SAPARD and ISPA will both stimulate labour demand in agriculture by

10. Russia and Ukraine form a third path, one of relatively little adjustment [see Swinnen, Dries and Macours (2003) for a discussion].

increasing productivity of farming and stimulate the outflow of labour by increasing alternative employment opportunities and by reducing labour mobility constraints.

To have an idea of how accession may affect this process it is useful to look at what happened with agricultural employment with the accession of Greece, Spain and Portugal to the EU. At the time of their accession to the EU, they had a large share of their population working in agriculture, as in the CEECs: 14% in Spain, 17% in Portugal and 29% in Greece.

Table 2 shows how the outflow of labour *increased* after accession of these southern countries. The strongest increase actually occurred in years 5-10 after accession. In this period, the average annual outflow in all three countries was 5% to 7%, annually. This is about the average outflow of labour in CEECs during the 1997-2001 period (see Table 1). The fact that the strongest outflow came with some delay after accession may also have been affected by the fact that these countries all had a transition period with accession. They did not enter the single market until several years after accession, and hence some of the pressures for restructuring and the benefits of increased job opportunities may also have arrived with some delay.

Table 2. Average annual change in EU agricultural employment (%)

	Spain	Portugal	Greece	ex-DDR	EU-15
5 years before	-3.5	-1.7	na	na	
1-5 years after	-5.2	-2.0	-1.0	-15.8	
5-10 years after	-5.4	-7.3	-4.7	-5.2	
10-15 years after	-1.2	3.0	-0.9	na	
1-10 years after	-5.3	-4.7	-2.8	na	
1-15 years after	-3.9	-2.1	-2.2	na	
1991-2001	-3.3	-2.2	-2.6	-12.2	-3.2

* Ex-DDR data until 1998.
Source: Own calculations based on ILO and European Commission.

It is also interesting to compare with labour adjustment in the former East Germany. The pattern of agricultural labour outflow in the ex-DDR is similar to the pattern followed by Estonia, Czech Republic and Hungary: a dramatic reduction in labour (-15% annually on average) during the first five years, and a more gradual, although still high (-5% annually), reduction in the next five years – which is similar to the CEH reduction in the 1997-2001 period.

These experiences suggest that the labour outflow from agriculture is likely to continue after EU accession. Whatever benefits may come from CAP subsidies, they are unlikely to offset the pressures and incentives for further, and significant, cuts in the agricultural labour force. The experiences also suggest that an increase in labour outflow may take place in those countries, where labour reductions have been relatively small.

This prospect should focus the attention of policy-makers in CEECs on implementing policies to facilitate this process in the framework of EU accession – and the use of EU support. Policies to enhance human capital of the rural labour force and to improve access to finance in rural areas are key aspects for labour mobility and rural development. Insufficient education and skills not only constrain management and productivity improvements in agriculture, but also the emergence of new rural

businesses, as well as the opportunity of unemployed workers (and underemployed labour on farms) to exploit employment opportunities outside agriculture.

Investment in education would contribute to several objectives, consistent with the overall objective of rural development, such as the improvement of productivity of existing enterprises, the growth of new enterprises, reduction of unemployment, and a shift of underemployed farm labour to other activities, thereby increasing labour productivity of the remaining farms. Investments to improve rural education could also reduce the incentives for young people to leave rural areas.

Finally, the development of rural infrastructure and of institutions for facilitating access to finance in rural areas, both for farms and non-farming activities, is important in order to encourage rural growth and employment opportunities. It should be an important focus for a rural development strategy.

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FACTORS THAT INFLUENCE LABOUR MOBILITY BETWEEN REGIONS AND COUNTRIES

By Dr. Marek Góra

Abstract

Labour mobility is one of the key factors determining GDP growth and enhancing welfare. Policies to promote greater labour mobility are a high priority in all countries and especially in transition economies. Greater flexibility in labour markets is essential in order to find an equilibrium between the supply and demand for labour. However, there are many economic, social and political constraints which tend to limit the movement of labour between regions in a country and between countries.

Introduction

The importance of labour mobility is quickly growing. It is one of the key factors determining growth potential of economies. Labour mobility is on the top of policy agendas all over the world, especially in Europe. The Lisbon Strategy of the European Union underlines this fact. Higher mobility is necessary to increase competitiveness of European economies and to allow them to compete with the US economy. Increasing mobility is even more important for transition and post-transition economies, where competitiveness is even weaker.

Labour mobility is one of the key challenges not only for economies, but also for modern societies. Until the 1970s (the time is country specific) mobility was much less important. Its importance grew afterwards as a result of an important change in economic development. Since then economic restructuring has ceased to be a from-time-to-time phenomenon and turned into an almost permanent process, a permanent restructuring.[1] This requires much more efficient reallocation of production factors, first of all reallocation of labour. In order to play their role efficiently, labour markets have to behave differently nowadays in comparison to previous situations. Labour supply needs to adjust to a quickly changing structure of labour demand, that in turn, follows changes in product markets.

European economies, transition economies in particular, need to adjust to these new circumstances. The situation in transition countries is more difficult since they also need to overcome weak economic structures inherited from the command economy. For instance, agricultural sectors in transition countries are usually larger (in terms of employment – not necessarily in terms of product) than in OECD countries.[2] So mobility is needed in transition economies due to two different reasons. The first is to fix inherited inefficiencies, and the second is to keep pace with economic developments of the 21st century.

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1. See Góra (2000).

2. The case of Poland – even if it is not typical for the region – illustrates the problem well. Employment share of agriculture is around 25% (depends on methodology of calculation) while the share of GDP produced in agriculture is slightly above 3%. These data show that the social component of the problem is more difficult than the economic component.

Agricultural policy in transition and post-transition[3] countries that are just in the process of joining the European Union is exposed to additional problems related to the application of the Common Agricultural Policy (CAP), that is in a process of change itself.

Labour mobility – basic framework for analysis

Labour markets allocate labour to production. If wages are flexible and reflect labour productivity, then in seeking the best paid jobs, people allocate in a way that maximises output. The question is whether wages really reflect productivity on one hand, and whether workers are aware of job opportunities, as well as can and wish to follow wage signals on the other hand.

People seek a job because they wish to earn more money in a new job, than in the one they have at the moment, or because they do not have any job at the moment (or expect to be laid off) and seek a job. In the latter case we can distinguish:

- New entrants.
- Laid-off workers.

Following wage signals, workers can seek jobs in “close” or “distant” places. Mobility does not require migrating. Jobs can be found in:

- Another firm.
- Another industry.
- Another sector.

In each case new employment can be found:

- Close to the worker’s place of permanent residence.
- Within the area close to the worker’s place of residence (commuting).
- In another region within the country (regional migration).
- Outside the home country (international migration).

Mobility, especially if it requires migration, depends on individual worker characteristics. Factors stimulating mobility, as well as factors slowing it down, create different effects, subject to numerous features of which the following ones are the most obvious:

- Age.
- Gender.
- Martial status.

3. Transition from command economy to markets is not endless. However, it is difficult to say when the transition is over. We can assume that some Central and Eastern European countries are post-transition ones.

- Education/skills.
- Currently available income.
- Owned property.

Labour mobility may mean leaving (layoff, quit) regular employment and entering irregular (shadow economy) employment. Incentives for such a change may stem from high tax wedges, and especially, the social security cost part of the wedge. This type of change can be particularly the case for migrants from rural to urban areas. Is it good or bad? In principle it is bad and should be avoided. On the other hand, we should weigh what is more dangerous – the "shadow" economy or agricultural over–employment? In the longer run there is no doubt, however, that the "shadow" economy should be reduced as much as possible.

Productivity, wages and social transfers

Productivity in agriculture is usually lower than in other economic activities. This can be explained in two ways. Agricultural family farms employ family members in many cases irrespective of whether they are needed or not. These farms can produce the same output with less employment. "Idle" workers productivity is zero, but since they remain on family farms, the average productivity is low. At the same time – due to technological reasons – it is difficult to achieve high productivity in agriculture even if employment could be kept at the optimal level. Effects of both factors add up, causing productivity in agriculture to be relatively low.

Lower productivity in agriculture than in other sectors causes lower income of agricultural workers and creates a pressure for migrating out of rural areas. This pressure is further increased by factors like:

- Expectations of a better life in urban areas.
- Expectations of better job opportunities in the future.

At the same time, the migration pressure is reduced by other factors, of which, the most important are:

- Costs of migration.
- Objective constraints.
- Subjective constraints.

Each of the above factors needs some explanation. It is provided in the next section.

Wage signals, expectations of benefits and costs depend on the information available to potential migrants. Workers often declare migration intentions based on the overestimation of its benefits, while their resistance against migration can also be based on overestimation of its costs. Actual migration decisions are not necessarily correlated with migration intentions expressed in various surveys.

Costs of mobility (migration) and other constraints

Direct money costs of mobility are not high. However, there are two types of indirect costs that can strongly affect individual decisions. First, the loss of family support (accommodation, foodstuff and so on). It is much cheaper to stay than to move and live in another place without family support. Second, the possible loss of social transfers that are usually targeted to those who stay, not those who move. In general, while social transfers play an important role, they can also create negative externalities. If they could be redesigned they would help to motivate people to be more mobile. Typical social transfer patterns freeze the current situation rather than help in changing it.[4]

From the objective constraints I would highlight the following:

- Availability of moderate housing for low/average paid workers.
- Administrative constraints.
- Overall economic situation (boom, recession).

From the subjective constraints I would highlight the following:

- Lack of skills (low educational attainment).
- Losing the social environment.
- High risk aversion.

In the case of international migration additional costs are usually taken into account, of which, the following are probably the most important:

- Foreign cultural environment (language, habits, and so on).
- Loneliness (family stays in the home country) or high costs of living (family migrates with the worker).

These are just some examples of costs and other constraints that reduce pressure on migration even if this pressure exists due to wage differentials.

Labour demand and labour supply

Economic growth depends on the employment of production factors. The more labour and capital employed and the higher their productivity, the larger the GDP. Employment of labour depends on its supply and demand. Paradoxically, nowadays shortages can be observed on both sides of the market. Demand cannot absorb the entire labour force. Many countries suffer from high unemployment. For the entire 1990s average unemployment in the EU was around 10%. At the same time labour supply, especially in developed countries, is shrinking due to demographic as well as welfare system related reasons. The average demographic dependency for the OECD area was 23.8 in 2000 and is projected to more than double, reaching 49.9 by 2050. For some countries *e.g.* Italy, Spain may reach more than

4. This is strongly based on the Polish experience, but applies to many other cases as well.

60.[5] The estimated cost of early retirement policies was above 7% of GDP and is projected to increase more than 9% of GDP in 2010.[6]

More employment is strongly needed, due to economic reasons, as well as social reasons. More employment is possible only if effective labour supply can increase and at the same time be absorbed by demand. However, labour demand depends on developments in product markets and technology, and can be adjusted by policies only on the margin of the market (subsidies) while more labour market flexibility (flexible wages, loose employment contracts) can help a lot, but is difficult to achieve.

While affecting labour demand (especially in the longer run) is difficult, the supply of labour can and should be adjusted. The number of people of active working age is determined by demographies, but effective supply depends on the activity of the population. It depends on many factors including tradition, health status, and availability of social transfers or child care (especially in the case of women). Productivity of labour depends on education, skills and technology. An increase in effective supply translates into stronger GDP growth, if labour demand is flexible enough to absorb the increased supply.

Supply and demand sides are subject to different factors, so they match each other only to some extent. Employment mismatch is one of the key labour market characteristics. If non-employment is taken into account then this mismatch can also be defined in a broader sense applying to inappropriate skills or residence of parts of the inactive population. This approach can be useful in analysing agricultural employment and policies aimed at agricultural reform.

In the past, especially in the nineteenth century, migrations from rural to urban areas were relatively easy in countries going through quick industrialisation at that time. Large numbers of new jobs were created in newly established factories. Many of the jobs were available for unskilled workers. Skills required for taking many other jobs were easy to acquire. At the same time, living standards acceptable to people migrating to urban areas were modest. The flow of migration from rural to urban areas was constrained mostly by the pace of industrial development.

The above situation is not often present, at the beginning of the twenty first century, in traditional industrialised countries or transition ones. Labour is not homogenous any more. Jobs are available for workers having certain characteristics. Very few job opportunities exist for unskilled workers. If such jobs exist they are low paid, hence they do not create strong incentives for workers to migrate in order to take these jobs. Education attainment and skills play the most important role. Traditional migration patterns are gone.

Labour supply can be better absorbed by labour demand, if the supply structure matches the structure of demand. A mismatch contributes to unemployment.[7] A reduction in this mismatch can be speeded up through well-designed labour market policies that focus on training. Actually, education is the most effective way to reduce this mismatch and increase employment, hence also to increase output (more employment, higher productivity).

Countries with high employment in agriculture have to solve a very difficult problem. This problem can even be dangerous for economies and their competitiveness. The problem can obviously be socially dangerous. They can increase effective supply of labour and consequently long-term GDP

5. See OECD (2002).

6. See Herbertsson and Orszag (2003).

7. See, for instance, Padoa Schioppa (1991).

growth. This requires very well designed education policy and improvement of labour market flexibility. Additionally, patience is also needed, as even if both requirements are 100% fulfilled, effects will not come soon.

International migrations

Taking a job in another country is more difficult and involves more costs than taking a job in one's home country, even if the latter requires migrating to another region. The difficulty stems from administrative procedures that need to be passed in order to take a legal job. Foreign workers are subject to much more strict regulations than domestic workers. However, this factor affecting migrations will soon cease to exist. Joining the EU means, among other things, free movement of labour, which means that workers in all member countries are treated the same. This will soon apply to workers from new member states, including workers from the Baltic States.

Free movement of labour is one of four key freedoms in the EU. However, there are some fears in many existing members of the EU. It is often expected that wage differentials, as well as high unemployment rates (in some accession countries), will push workers from new member states to "invade" old member countries' labour markets, which in turn, is expected to create problems. This is why some countries imposed transition periods on the free movements of labour. This situation needs some further explanation.

First, the reasons for migrating are much weaker in comparison to what can be expected after comparing wages and unemployment. The average wage applies to the entire population, of which, only a fraction is able and willing to migrate. Those workers who could migrate are usually younger, better educated and usually earn more than the average. Moreover, they usually have good career prospects in the home country. They may plan on working abroad, but their desire to do so is not as strong as it is usually assumed. The rest of the population, including the unemployed, may strongly wish to move abroad and take jobs there, but their ability to be legally employed is low. Illegal employment; this is another story, but it has nothing to do with changes that are expected after joining the EU. Actually those who were determined enough to take "shadow" economy jobs in EU countries are already there. They would probably not get any job if their employers had to pay the full costs of their legal employment. So paradoxically expectations on legal employment of workers from new member states, resulting from joining the EU by these countries, are based on evidence related to illegal employment of workers from these countries.

Second, we should ask the question whether it would be really difficult for the old EU member states if more people from new member countries take legal employment in the EU. The answer to this question is three-fold. Inflexible European labour markets will hardly absorb new workers, migrants from new countries will not substantially affect the labour market situation. However, if these markets reacted to an increase in the labour supply then wages would go down (ceteris paribus). This may not be satisfactory for many workers, but would contribute to stronger growth, which is needed in many EU countries. The last part of the answer is probably the most important. Pension systems in a majority of EU countries have deep financial problems. Dependency ratios are very high (few contributors, numerous beneficiaries, high generosity of benefits). Legal migration into the EU would contribute to easing the financial problems as migrants are usually young. They will keep contributing for many decades before they start receiving any benefits. From this viewpoint, migration from new member states to the old ones would be good for the latter countries, but bad for the CEECs.

Final remarks

Labour mobility is nowadays one of the key factors determining the growth potential of economies. Labour mobility can also be difficult for most people. Well-designed policies could and should be used in order to help them. This applies to all kinds of mobility. Institutions and regulations have to contribute to an increase on mobility.

Education is the most important, effective in the long run, precondition for efficient allocation of labour and consequently for competitiveness and growth of modern economies. Training programmes can additionally help and provide results in the short run. People, especially younger workers, can also get other help *i.e.* education for change, or creation of greater ability to adjust. The goal is to help people in taking a decision to move rather than to stay – in current firm, profession, region, and so on – if needed.

Moving job opportunities to rural areas creates an option for mobility without migration. This reduces the problems faced by people in rural areas. Post industrial demand for various services based on tourism and other activities in urban areas creates a strong push in this direction. Also in this case, well-designed policies can help and generate a lot of economic, social and cultural positive externalities.

In order to find new jobs, agricultural workers have traditionally changed employment to other sectors that required migration to other regions or countries. Nowadays rural development funds provided by governments, as well as international organisations help agricultural workers adjust, but not necessarily move out of the place of their residence. This creates a much better environment for labour mobility and reduces the costs of migration both to individuals and to society.

Modernisation of economies, if this is accompanied by improvement of infrastructure, can contribute to using yet another possibility; namely, movement of non-agricultural firms and their workers to rural areas. This would be possible in selected high-tech firms, especially those operating through Internet. This requires well-developed telecommunications, road systems (people cannot be cut off from urban areas), availability of schools (nobody would accept sending his/her kids to small schools offering weak education), and appropriate policy measures.

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DEVELOPMENTS IN THE LABOUR MARKET AND LABOUR MOBILITY: THE CASE OF ESTONIA

By Ms. Kaili Järv

Abstract

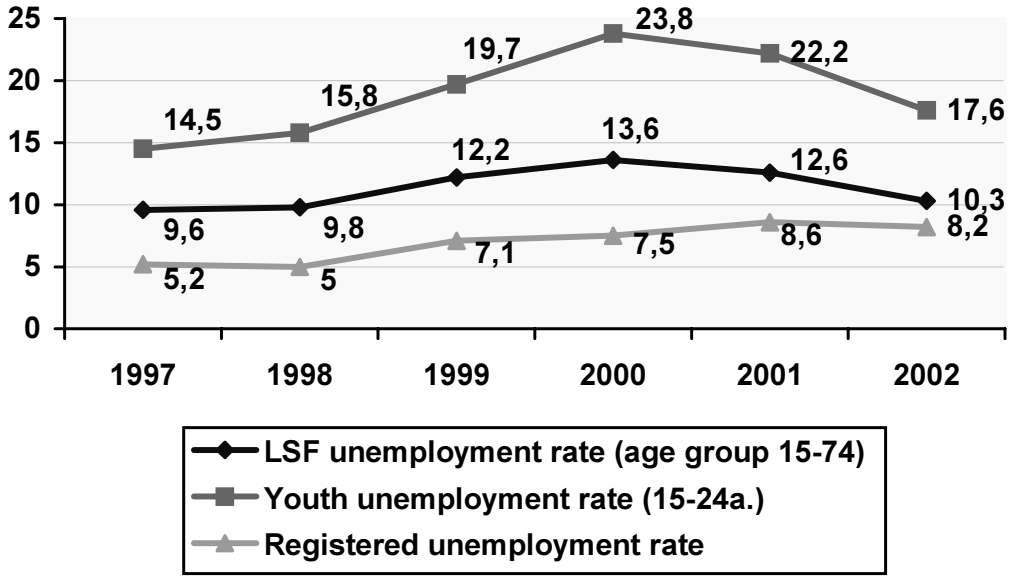
In modern economic literature labour mobility is usually considered in the framework of labour market flexibility, which in turn is strongly related to the issues of structural imbalances in the labour market. The most significant concerns in the Estonian labour market are big regional (and centre-periphery) differences of participation and employment although the country is small by area. In addition, large-scale structural changes in the Estonian economy have resulted in mismatches between the skills of the labour force and job vacancies. The key word 'structural unemployment' is therefore the focus of labour market policy and probably will stay there for some time. When designing new policy measures, which allow for more flexible labour markets, it has to be kept in mind that only regionally balanced development can ensure sustainable welfare for the entire population. This paper analyses the extent of regional differences in the Estonian labour market and the potential of the different types of labour mobility in levelling the imbalances.

The paper consists of two parts. Firstly, an overview of labour market developments in Estonia will be given including, labour division between different sectors of the economy, as well as geographically. Besides, the topic of labour market flows between the three labour market states of employment, unemployment and non-participation will be discussed, as a type of labour mobility. Secondly, the underlying factors and policy measures affecting labour mobility in rural areas will be described and discussed.

Overview of labour market developments in Estonia

Recent economic growth has brought along positive changes in the labour market. Employment improved significantly in 2002. The unemployment rate, which was the highest in 2000 (13.6%) decreased to 12.6% in 2001 and to 10.3% in 2002 (Figure 1). Although, the number of discouraged persons also decreased for the first time in 2002, the economically inactive population is still growing in Estonia. Labour market flows between the three labour market states of employment, unemployment and non-participation have also been analyzed in Estonia on a regional level (Eamets, 2003), which provides useful information about the factors underlying labour mobility in Estonia.

Figure 1. Dynamics of unemployment rates in 1997-2002



Source: *Labour Force Survey*, Labour Market Board.

Regional differences in unemployment in Estonia are significant. Broken down by county, unemployment rates can vary two to three times. For years the highest unemployment rates have been in the industrial region in Northeast Estonia and in the agricultural region in Southeast Estonia. By county, the unemployment rate varied in 2002 from 5.8% in Tartu county to 18.9% in Ida-Viru county.

In order to get a comprehensive review of labour market developments on the regional level, it is important to look at both the dynamics of unemployment, as well as activity rates. People can move from unemployment to employment or non-active status (Table 1).

Table 1. Activity rate, employment rate and unemployment rate of population aged 15-74 by regions* 1998-2002

(annual average, percentages)

	1998	1999	2000	2001	2002
Northern Estonia					
Activity rate, %	68.8	68.3	67.9	68.3	67.8
Employment rate, %	62.6	61.3	60.1	60.4	62.0
Unemployment rate, %	9.1	10.2	11.5	11.6	8.6
Central Estonia					
Activity rate, %	62.3	61.3	60.7	63.0	60.6
Employment rate, %	57.1	53.9	51.6	56.0	54.7
Unemployment rate, %	8.4	12.0	14.9	11.0	9.7
Northeastern Estonia					
Activity rate, %	62.0	61.2	61.9	60.6	60.7
Employment rate, %	52.9	49.0	48.8	49.7	49.2
Unemployment rate, %	14.7	20.0	21.1	18.0	18.9
Western Estonia					
Activity rate, %	63.3	59.8	61.2	59.6	60.0
Employment rate, %	58.3	52.7	54.0	53.1	54.4
Unemployment rate, %	7.9	11.8	11.8	11.0	9.2
Southern Estonia					
Activity rate, %	58.6	57.9	58.8	57.8	56.3
Employment rate, %	52.7	51.2	50.9	50.5	51.1
Unemployment rate, %	10.0	11.6	13.4	12.8	9.3
TOTAL ESTONIA					
Activity rate, %	64.0	63.0	63.3	63.1	62.3
Employment rate, %	57.7	55.3	54.7	55.2	55.9
Unemployment rate, %	9.8	12.2	13.6	12.6	10.3

* Northern Estonia: Harju county (incl. Tallinn);
Central Estonia: Järva, Lääne-Viru and Rapla counties;
Northeastern Estonia: Ida-Viru county;
Western Estonia: Hiiu, Lääne, Pärnu and Saare counties;
Southern Estonia: Jõgeva, Põlva, Tartu, Valga, Viljandi and Võru counties.
Source: Data of the *Estonian Labour Force Survey*, Statistical Office of Estonia.

Studies have shown that in spite of improvements in unemployment and employment rates the proportion of unemployed and inactive persons to total working-age population (non-employment rate) shows a clear growing trend in every county (Eamets, 2003, pp. 190-191). Therefore, it is necessary to look also at the labour force participation rate and number of people who are inactive to find out whether the unemployed have moved to employment or inactivity.

One of the factors describing labour market flexibility is labour mobility between the different sectors of the economy. Employment rates in the primary sector have been decreasing throughout the transition period in Estonia. In 2002, 7% of employed persons worked in the primary sector (9% in 1998, 18% in 1992). The share of the secondary sector has been about one-third since 1993. The share of the tertiary sector in employment grew to 62% in 2002 (58% in 1998, 46% in 1992). Estonia is one of the candidate countries whose employment structure by economic sector resembles most closely that of the European Union.

Table 2. Employment by sector of economy, 1998–2002, urban and rural areas*

	1998	1999	2000	2001	2002
Agriculture	8.9	8.1	7.2	6.9	6.9
Industry	33.1	32.1	33.3	33.0	31.3
Services	58.1	59.8	59.5	60.1	61.7
Total	100.0	100.0	100.0	100.0	100.0

* Data of the *Estonian Labour Force Survey*, Statistical Office of Estonia.

Clearly, the distribution of employment between sectors differs in rural and urban areas. While the agricultural sector forms only 1.7% in urban areas, in rural areas 1/5 of the work force is engaged in agricultural activities. On the other hand, employment in the service sector is roughly 17% higher in urban compared to rural areas (Tables 3 and 4).

Table 3. Employment by sector of economy, 1998–2002, urban areas*

	1998	1999	2000	2001	2002
Agriculture	1.9	1.5	1.5	1.8	1.7
Industry	35.0	34.0	34.9	34.7	31.7
Services	63.1	64.5	63.6	63.5	66.6
Total	100.0	100.0	100.0	100.0	100.0

* Data of the *Estonian Labour Force Survey*, Statistical Office of Estonia.

Table 4. Employment by sector of economy, 1998–2002, rural areas*

	1998	1999	2000	2001	2002
Agriculture	26.6	24.4	21.4	19.9	20.6
Industry	28.3	27.5	29.4	28.6	30.3
Services	45.1	48.1	49.1	51.5	49.1
Total	100.0	100.0	100.0	100.0	100.0

* Data of the *Estonian Labour Force Survey*, Statistical Office of Estonia.

From tables 5 and 6 below it can be seen that the place of residence has significant influence on people's employment opportunities. Both the activity as well as the employment rate for the city population is 7% higher than those living in the countryside. Besides, in rural areas, discouraged persons make up a higher proportion of the inactive population than in urban areas. In 2001, about one-tenth of the inactive rural population aged 15-74 were discouraged persons, the corresponding figure for the urban population being only 5%.

Table 5. Labour force participation, employment and unemployment rates in 2001 by place of residence*

	Labour force participation rate	Employment rate	Unemployment rate
Total	63.1	55.2	12.6
City	65.2	57.2	12.2
Countryside	58.5	50.6	13.4

* Data of the *Estonian Labour Force Survey*, Statistical Office of Estonia.

Table 6. Employed persons by the sector of economy by regions, 2001, percentage*

	Northern Estonia	Of which Tallinn	Central Estonia	North-eastern Estonia	Western Estonia	Southern Estonia	Total
Primary sector	1.6	...	16.5	2.7	13.6	11.6	6.9
Secondary sector	29.7	29.3	30.7	51.5	35.1	29.2	33.0
Tertiary sector	68.7	70.3	52.9	45.9	51.2	59.1	60.1

* Data of the *Estonian Labour Force Survey*, Statistical Office of Estonia.

As mentioned above, it is highly important to observe in which direction people are heading both within employment, as well as between different states of the labour market. According to the analysis presented in (Eamets, 2003), the Estonian labour market generally is characterized by the following tendencies:

- Men leave the labour market to unemployment more often than women and women leave the labour force and become non-active more often than men.

- Education and qualifications play an important role in avoiding unemployment. ‘White-collars’ become unemployed only half as much as ‘blue-collar’ workers.

- Most people change from a previous sector of the economy to the service sector. Movements from other sectors to agriculture are practically non-existent, which relates to the fact that employment in the primary sector is relatively stable or decreasing and new workplaces do not arise very often.

- Young people are more mobile than the average, also in moving between different labour market states, including from employment to unemployment or inactivity (studies).

- The non-Estonian speaking population becomes unemployed more often compared to Estonians. At the same time, Estonians become more often inactive. The non-Estonian speaking population change jobs within the secondary sector (industry) and the Estonian workforce within the tertiary sector.

Still, besides these broad results, each regional labour market in Estonia has its own specific characteristics (Eamets, 2003):

North Estonia

The capital city, Tallinn, has always had a higher living standard, with a dominating service sector and higher employment rates. Compared to the Estonian average, in Tallinn and in its surroundings the differences between Estonians and Non-Estonians are smaller than in other regions. Persons who have been working in agriculture become non-active rather than looking for another job and many people move to the service sector. The impact of the level of education and qualifications on employment opportunities is even stronger than the average.

Central Estonia

Among the persons who move to the service sector, most are women. The proportion of agriculture is relatively big (20% of men and 14 % of women have changed workplaces within this sector). Most of the people who become unemployed or inactive worked previously in industry.

Northeast Estonia

The secondary sector is dominating. Women are mostly working in the service sector and men in the industrial sectors. Also, these movements are common within these sectors. Compared to the average, less people move to the tertiary sector (as few jobs are created).

Western Estonia

Compared to other regions, more people leaving the agricultural sector become unemployed – 5.5% (only Ida-Viru county is comparable). At the same time, more people are moving to inactivity, rather than staying unemployed.

Southern Estonia

Southern Estonia has for a long time been considered, together with Northeast Estonia, as a less developed region. This is supported by the fact that people tend to become more often non-active and do not continue searching for work.

Factors and policy measures affecting labour mobility in rural areas

Labour mobility in the context of labour market flexibility can take several forms *e.g.* people can move between different sectors of the economy and/or geographically. In recent literature, the analysis of flows between the three labour market states of employment, unemployment and non-participation has gained significant importance.

In Estonia, the leading analyst of labour market flexibility and labour mobility is Mr. Raul Eamets from Tartu University, whose results of the analysis of labour mobility between different labour market states and sectors of the economy have been referred to above.

Geographically, the Estonian population is considered quite rigid *i.e.* people do not leave their home-region very easily to work and live somewhere else with some exceptions within the younger and more educated groups (Eamets, 2003), which is probably one of the factors behind the regional disparities. The geographic mobility of Estonian people is limited mainly by economic factors (too

expensive to change place of residence), but also social factors are influential (difficulties with adapting to the new environment and leaving own social network). In the Estonian case, the language barrier and cultural differences are obstacles when moving from or into the Northeastern part of Estonia, where most of the population is Russian-speaking.

The main goal of the Estonian economic policy is to ensure sustainable, socially and regionally balanced economic growth. As long as Estonia faces remarkable gaps in development and income levels across regions the problem of structural unemployment is not going to disappear without well-focused policy intervention.

In accordance with the strategy for regional development in Estonia, none of the counties should have unemployment (measured in compliance with ILO methodology), in excess of the Estonian average by more than 35%. In 2002, altogether in the four counties the unemployment rate exceeded the average rate of Estonia (10.3%) by more than 35%.

The 2003 Progress Report of the JAP (Joint Assessment of Employment Priorities) in Estonia concluded that to replace the regional differences in the unemployment rate, it is essential to keep implementing the regional programmes, and through entrepreneurship policy to foster the creation of new jobs.

Employment policy that aims at improving the quality of the labour force and eliminating the mismatch between the existing labour force and job vacancies needs more efficient education systems, as well as increased and more focused use of active labour market measures for training and retraining the unemployed.

Labour market policy in Estonia is carried out in counties by employment offices subordinated to the Ministry of Social Affairs. They mediate jobs and offer various labour market measures to the unemployed. Tripartite councils at employment offices should have a vital role in fostering employment in regions.

With the help of different labour policy instruments one can enhance the geographic mobility of people (reduce the barriers of labour mobility) or the mobility of workplaces (subsidize job creation in less developed regions). The necessary extent of using these instruments depends on the country's ultimate goal. When regionally balanced development is the focus, then probably more intervention from the government level is needed. When flexibility of the labour market is considered to be the key to economic growth and, therefore increased welfare, then policy usually follows market forces.

According to the analysis based on public opinion polls in 2002 (Järv, Korts 2002) the Estonian population considers Estonia's policy instruments too oriented on enhancing labour mobility between regions (mostly to urban areas), at the same time, people would prefer policies that pay more attention to local development rather than promotes a change in the place of living and working.

Estonian regional policy is based on the principles of the EU regional policy. The strategic base document for regional policy is "The Strategy of Regional Development in Estonia" (1999), forming the basis for the programmes approved by the Government: the development of agricultural and industrial areas; support for the islands; the creation of a network of centres to promote local initiatives and cross-border co-operation; and the diversification of the economic structure of the Setomaa (south-east) region. Programmes are generally targeted at combating a further polarisation of the national economy and preventing associated macroeconomic problems.

Entrepreneurship activity is lower in Estonia than in the more developed European countries. Besides there is a disparity between the capital and the rest of the country – almost half of the enterprises are located in Tallinn and in its vicinity, and the trend continues. Therefore, different activities are being planned to promote entrepreneurship in all regions in order to generate the interest of potential entrepreneurs and provide information on available consultation services and training support in case of the lack of knowledge on how to start and manage a business.

Conclusions

Although recent economic growth has brought along positive changes in the labour market, the economically inactive population is still growing in Estonia. The regional differences in unemployment in Estonia are significant. Broken down by county, unemployment rates can differ two to three times. For years the highest unemployment rates have been in the industrial regions in the Northeast of Estonia and in the agricultural region in Southeast Estonia. As expected, a person's place of residence has a significant influence on his/her employment opportunities. Both the activity as well as the employment rate for the city population is 7% higher than those living in the countryside. Besides, in rural areas, discouraged persons make up a higher proportion of the inactive population than in urban areas.

The geographic mobility of Estonian people is limited mainly by economic factors (too expensive to change place of residence), but also social factors are important (difficulties with adapting to the new environment and leaving ones own social network). In Estonia, the language barrier and cultural differences are obstacles when moving from, or into the Northeastern part of Estonia, where most of the population is Russian-speaking.

Regional cohesion can be obtained through developing a better focus in relation to regional aspects of employment policy in order to concentrate more closely on the regions worst affected by unemployment.

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LABOUR MARKET DEVELOPMENT IN RURAL AREAS OF LATVIA

By Ms. Ginta Uzulina and Mrs. Aija Vucane
(Paper presented by Mrs. A. Vucane)

Abstract

The report describes the trends in employment and unemployment in agriculture and rural areas, as well as employment policy in Latvia. The main objective of this report is to give an overview of the labour market and factors affecting employment in rural areas of Latvia. The main features of employment in rural areas are: employment in agriculture is the main activity and source of income in rural areas in Latvia. A significant share of those employed in agriculture and in rural areas is ageing rapidly due to the movement of young people to cities, and the still limited possibilities to find a job in other sectors of the economy. The second objective of this report is to explain policy targets and measures promoting employment, as well as to evaluate the efficiency of these measures.

The labour market situation

Introduction

In Latvia the two main sources of data available for analysis of the labour market are: registered data, which are obtained from the State Employment Service (SES) and the other one is the Labour Force Survey (LFS). The LFS was first launched in November 1995 and was carried out twice a year, in May and November until 2001, with the objective to obtain detailed information about the labour market in Latvia and the economic activities of the population.

In 2002, the results of the LFS were available for each quarter. Starting in 2002, and in accordance with the regulations of the Statistical Office of the European Communities (EUROSTAT), Latvia started the uninterrupted survey, which is carried out weekly during the year in households, selected according to certain criteria. The methodology of the LFS is based on the methodology of the International Labour Organisation (ILO). The same methodology is also used in EUROSTAT and by the Organisation for Economic Co-operation and Development (OECD).

In this report, data and information from both sources are used, as well as additional information, which was summarised by the Central Statistical Bureau of Latvia. This information was requested by the Ministry of Welfare, in order to estimate trends in the labour market, especially in agriculture and rural areas.

Labour market developments in Latvia

At the end of 2002, the total number of economically active persons in Latvia was 1.1 million. This marks a reduction of 2% since 1998. The percentage split between male (51.6%) and female (48.4%), is almost equal.

Describing the labour market development, it is necessary to indicate that in 2002 the activity rate was about 62% in the age group 15-74. In rural areas, the economically active population comprises 59.3% of the total rural population (in urban areas it was 62.9%).

Comparing the economically active population in rural areas by sex, the share of males in rural areas (about 55% of the total economically active population in rural areas in 2002) was higher than females, and this share is increasing, gradually.

In order to characterise employment possibilities in rural areas by regions, the share of the economically active population employed, is used.

Table 1. Share of the population employed in rural areas and regions of Latvia, 1998-2002, %

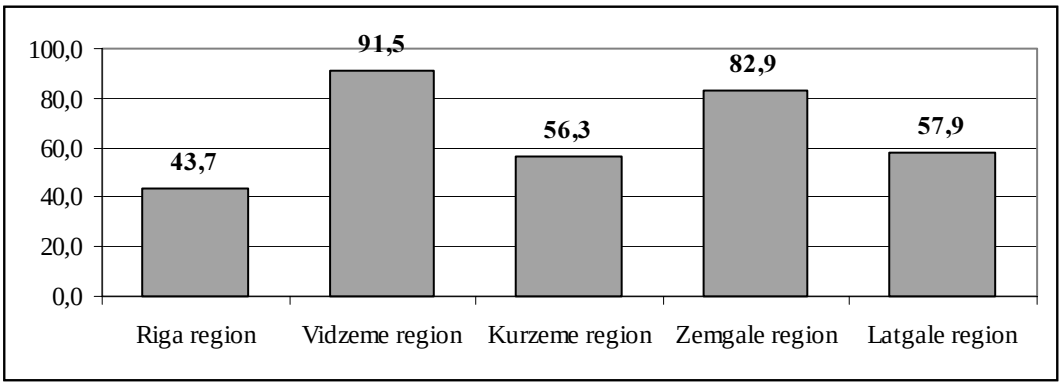
	1998	1999	2000	2001	2002
Riga region	93.0	88.2	90.9	92.2	97.3
Vidzeme region	92.7	91.6	88.7	88.7	90.9
Kurzeme region	93.5	93.6	90.1	90.0	91.6
Zemgale region	91.9	89.6	90.5	91.7	91.2
Latgale region	90.9	83.7	85.0	86.5	85.6

Source: Central Statistical Bureau.

As can be seen in Table 1, the best situation is in the Riga region, especially in 2002 and the lowest share of employment was in the Latgale region. A high level of this indicator can be explained by the definition of employment as used in the LFS. A big share of those employed in rural areas has to work part time, because of seasonality and other reasons.

Comparing the labour force (the number of economically active in the population), the highest level of economically active people is observed in the Vidzeme region. In 2002, it was 91 500 people -about 28% of the total economically active population in Latvia.

Figure 1. The economically active population in rural areas and regions in 2002, '000

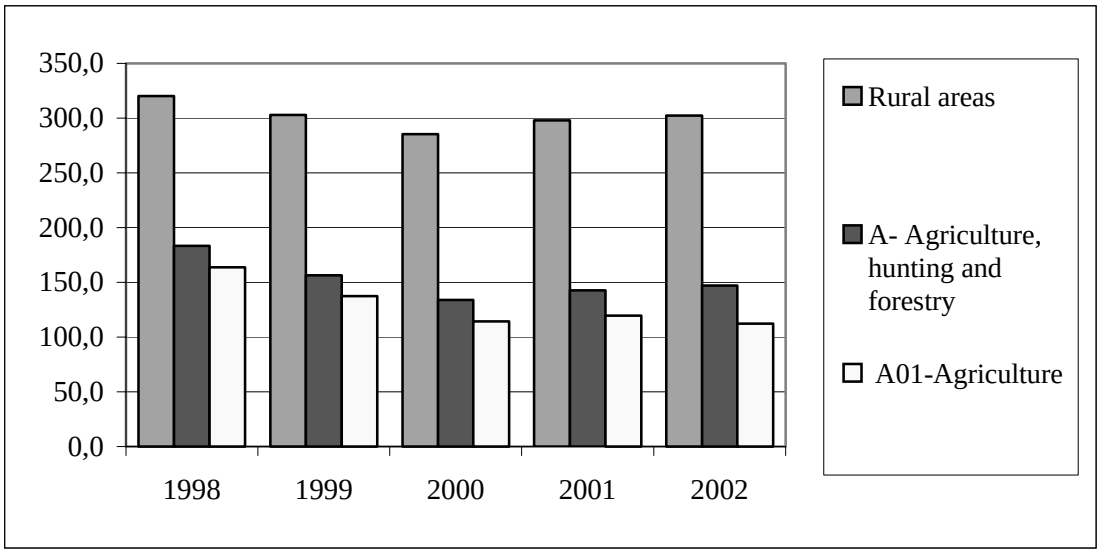


Source: Central Statistical Bureau.

Employment in agriculture and rural areas

The number of people employed in agriculture, hunting and forestry increased slightly, as did the average in the whole economy. This is a positive tendency and is due to several reasons.

Figure 2. Population employed (annual average) in rural area and agriculture in 1998–2002, '000



Source: Labour Force Surveys.

Analysing the number of persons employed in agriculture indicates a decline, which shows that workers move from agriculture to other sectors and especially the forestry sector. The number of persons employed in rural areas has been increasing since 2001; this also indicates some movement of workers from agriculture to other sectors.

The employment rates in Latvia differs significantly by region (NUTS III level) due to the uneven social and economic development. Regional mobility as an important instrument for balancing the demand and supply for workers is pretty complicated at present, due to infrastructure and housing provisions. Comparing employment in agriculture and rural areas in different regions, the figures show that the number of persons employed in agriculture in 2002 is the highest in the Zemgale region. It is necessary to emphasise that Zemgale is a typical agricultural region with good quality soil and this could explain the high number employed in agriculture in this region.

In the Riga region, the number employed in agriculture has remained stable in recent years but, for example, in Kurzeme and Latgale, as well as in the Zemgale region the number employed in agriculture decreased. In 2002, only in the Vidzeme region has the number increased. This shows that employment in agriculture vary between different regions, even from year to year. It is difficult to explain the reasons for this movement between different regions. It could be useful to study these changes and factors to define more effective policy for labour mobility in rural areas and regions.

Table 2. Number employed in agriculture in the different regions of Latvia in 1998-2002, '000

Regions	1998	1999	2000	2001	2002
Riga region	11.2	9.5	8.3	9.3	9.3
Vidzeme region	44.7	40.7	29.5	26.6	29.2
Kurzeme region	27.5	26.7	21.4	21.2	17.2
Zemgale region	47.0	36.5	33.5	35.6	32.5
Latgale region	33.5	24.0	21.9	27.1	24.0

Source: Central Statistical Bureau.

If one compares the share of the population employed in agriculture with the total number employed in rural areas by regions, the largest proportion is in the Latgale region (Table 3). This indicates that in this region almost half of the employed population is involved in agricultural activities and agriculture is the main source of income for many households in the region. The possibilities for other types of economic activities are still limited in the Latgale region. The state and local government policies should be targeted to fostering possibilities to start other economic activities in the Latgale region.

The next largest share of agriculture employment is in the Zemgale region, but in this region agriculture is a traditional economic activity.

Table 3. Share of population employed in agriculture in rural areas and regions of Latvia in 1998-2002, %

Regions	1998	1999	2000	2001	2002
Riga region	26.8	22.4	22.0	22.9	21.9
Vidzeme region	51.3	47.0	38.1	33.7	35.1
Kurzeme region	50.9	50.7	43.1	44.7	33.3
Zemgale region	58.9	51.0	46.6	46.9	43.0
Latgale region	58.3	48.3	45.3	49.1	48.4

Source: Central Statistical Bureau.

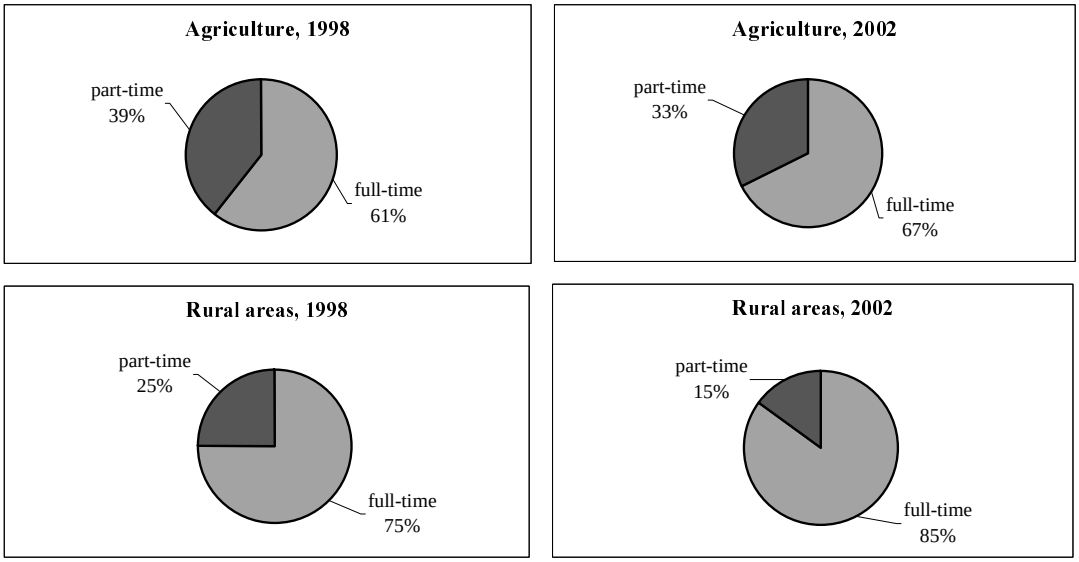
Even if the share of the population employed in agriculture in rural areas of the Latgale and Zemgale regions are similar, the reasons for this are quite different. For example, the number of unemployed persons and share of job seekers in rural areas in Latgale and Zemgale region discloses interesting differences between these regions.

In 2002, the share of job seekers in the economically active population in rural areas was 14.3% in the Latgale region and 8.8% in the Zemgale region. Many inhabitants of Zemgale have found suitable employment in Riga and they commute to the capital every day, returning to the region in the evening. Moreover, the most fertile soils are in the Zemgale region. But, in the Latgale region - several households, particularly in rural areas, subsist on farming, on old age pensions of elderly family members and child allowances. Further, eastwards – soils become more and more unfertile and unsuitable for agriculture. This explains why employment in agriculture are almost similar in these two regions, but regional development shows that for each region this indicator is influenced by different factors.

Employment and working time

It is necessary to highlight that a very high proportion of people employed in agriculture are working part-time. For example, in 1998, the share of those employed, which worked part-time was 39%, but in 2002, this figure had fallen down to 33%. Comparing employment in rural areas, the share of part-time employment was 15% of the total rural working population. These figures show that the number of part-time workers is decreasing, which is a positive tendency in the labour market in rural areas (Figure 3).

Figure 3. Employment in rural areas and agriculture by working time in Latvia in 1998 and 2002, %

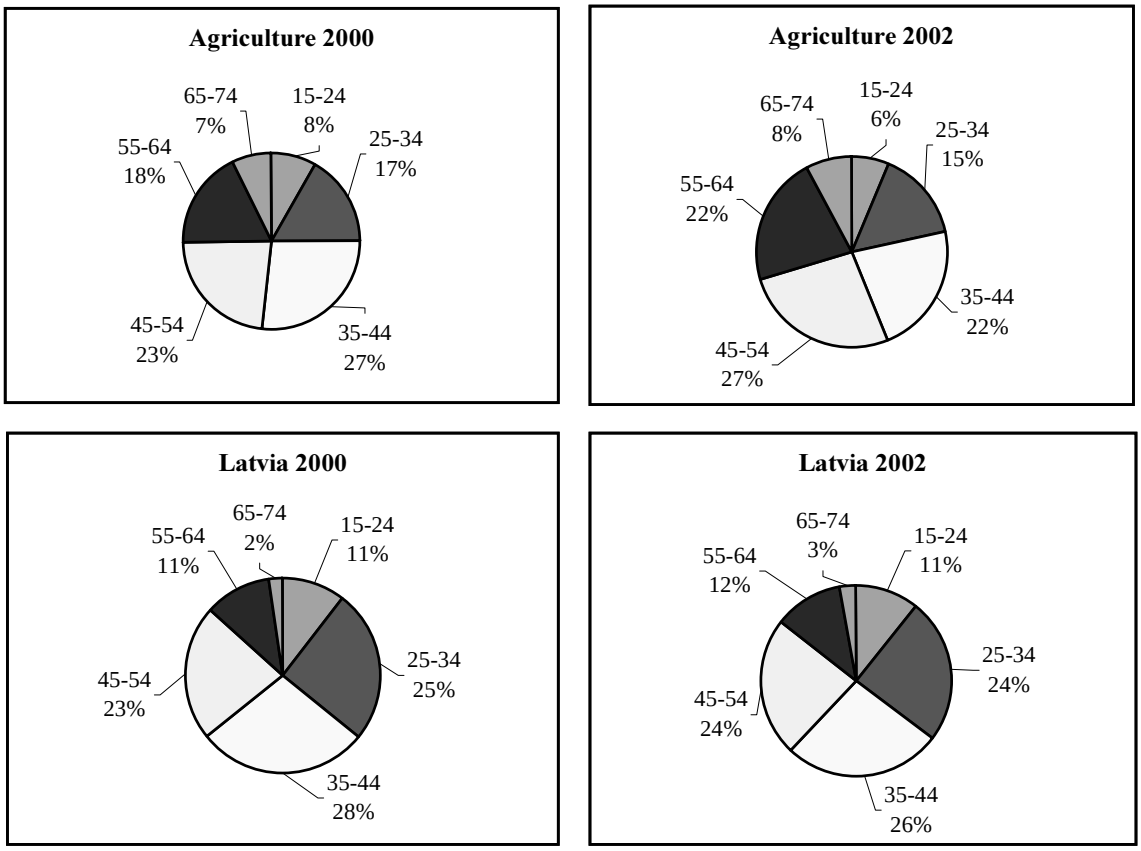


Source: Central Statistical Bureau.

Employment and age structure

Comparing the age structure between those employed in agriculture and employment in the whole economy, shows that a significant share of those employed in agriculture is between 55 and 74 years old. In 1998, it was about 25% of the total number employed in agriculture, but in 2002 the share rose to 30%. The share of population employed in the age group 55-74 years was about 13% and 15%, on average, in 1998 and in 2002 respectively (Figure 4). There are several reasons for this trend in the structure of employment. The ageing of the workforce in agriculture is more rapid than for the population, on average. This also suggests that many people move to cities, where it is possible to find new jobs. But older people stay in the countryside and this factor influences employment and the structure of employed in rural areas and in agriculture.

Figure 4. The structure of employment in agriculture and the average number employed in 2000 and 2002, %



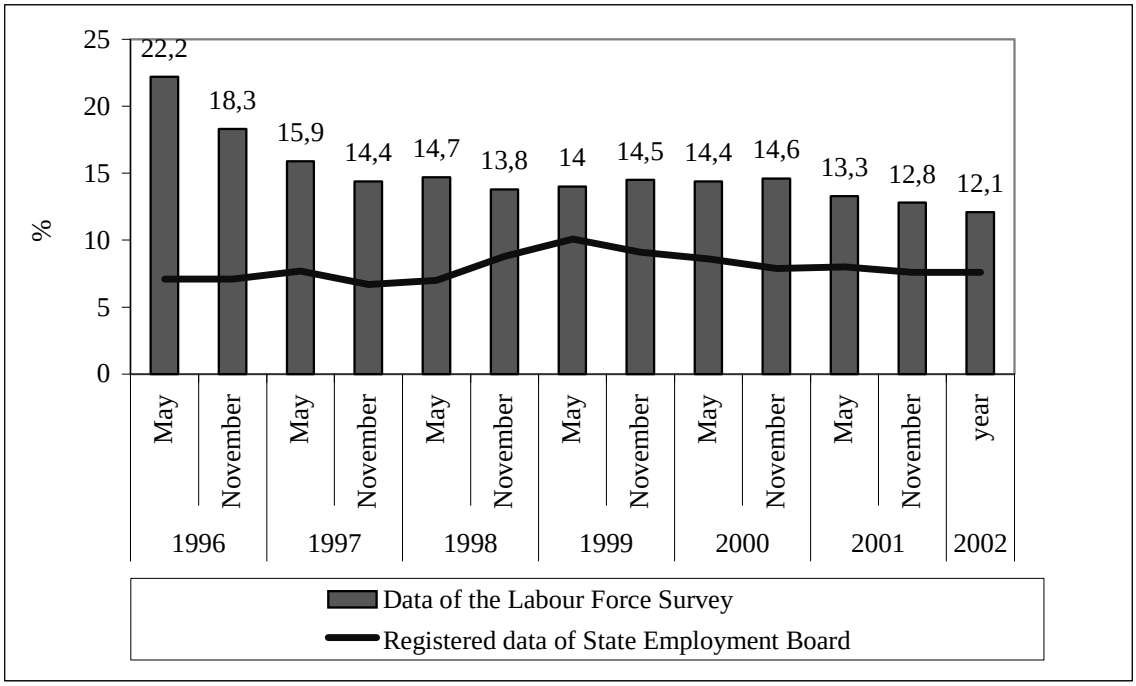
Source: Central Statistical Bureau.

This also means that there are limited opportunities for employment and income in other sectors. Depression, insufficient and uncoordinated rural support policies are contributing to the outflow of the economically active, higher qualified rural population and youth to the bigger towns of Latvia (Riga, in particular). This accelerates the ageing of the rural population.

Unemployment

The unemployment rate in Latvia in 2002 was 12% (women – 11%, men – 12.9%). This rate has decreased over the last three years, but still is considerably higher than the EU average. Only 7.6% had been registered, officially, in the State Employment Service as unemployed.

Figure 5. Unemployment rate in Latvia 1996-2002, %



Source: Central Statistical Bureau.

The limited capacity of the State Employment Service to provide services to the unemployed is one of the main reasons for the low registration of unemployed persons. A significant proportion of the unemployed is out of work for long periods. About 46% of the unemployed had been out of work for over one year in 2002. The level of long-term unemployment has been rather stable over recent years but in 2001, a positive tendency was observed. The highest share of long-term unemployed was in several districts of the Latgale region, with more than 50% of registered unemployed.

Hidden unemployment is more widespread in rural areas. For example, the proportion of family members involved in unpaid work is 14% in rural areas, but 0.3% in towns. The proportion of underemployment in 2001 was estimated at 8.5% in rural areas, but only 4.0% in towns (Table 4).

Table 4. Underemployment, %

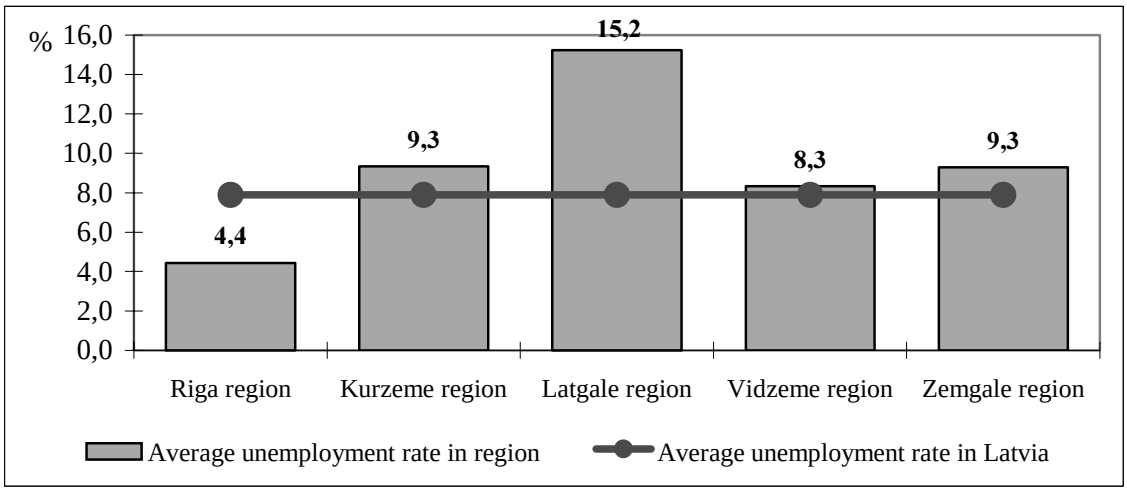
	1998	1999	2000	2001	2002*
A- Agriculture, hunting and forestry	17.0	17.8	17.4	12.7	2.5
Of which: Males	20.0	20.3	20.1	13.9	3.2
Females	12.8	14.5	13.8	10.7	1.3
A01- Agriculture	17.9	18.5	18.4	13.4	2.5
Of which: Males	22.2	22.0	22.5	15.4	3.3
Females	12.9	14.7	13.7	10.7	1.4
Rural areas	12.7	12.4	11.8	8.5	1.6
Of which: Males	15.2	13.4	13.5	9.7	2.2
Females	9.8	11.3	9.7	7.1	0.9

*Definition of underemployment changed (see Annex 1).
Source: Central Statistical Bureau.

The high tax burden represents a significant barrier to the creation of jobs at moderate wages, and is a disincentive for many of the unemployed to take up jobs. Moreover, a high marginal rate of income tax (for employees 25%) and social contributions (for employers 24.09% and for employees 9%) are likely to promote employment in the "grey economy" (according to the Central Statistical Bureau of Latvia the “grey economy” in 2001 was 17% of GDP, but according to the Ministry of Finance it reached 25% of GDP).

The unemployment rate varies significantly between regions. As compared with the overall unemployment rate of 12% in 2002, unemployment was higher in Kurzeme and, particularly in, Latgale. The underlying trend over the last five years has been for unemployment to fall in Riga and Zemgale, but to remain persistently high in Latgale.

Figure 6. Unemployment rate in different regions of Latvia in 2002, %



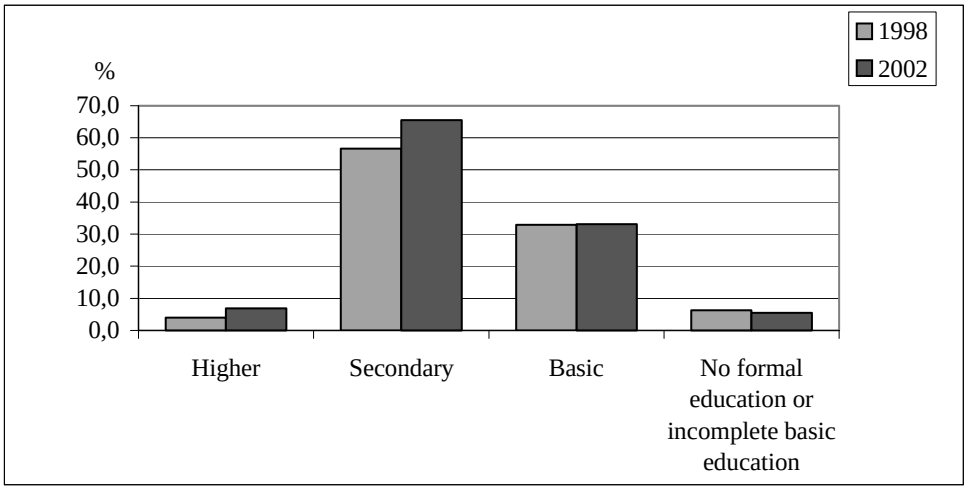
Source: Central Statistical Bureau.

Main factors effecting employment

Employment and education

One of the reasons for the low economic activity in rural areas is the insufficient level of knowledge and skills. These would not correspond to the principles of modern market economies to satisfy the demand for healthy and safe food production that requires specialised knowledge. A similar situation prevails among the owners of private forests and foresters, who lack the knowledge about sustainable forest management and the wood market. A correlation is observed between job seekers and the education level in rural areas. There is a tendency that the largest share of job seekers has only secondary education, which means that in rural areas more specific professional knowledge could be useful, in order to find a job or to start other enterprises in rural areas (Figure 7).

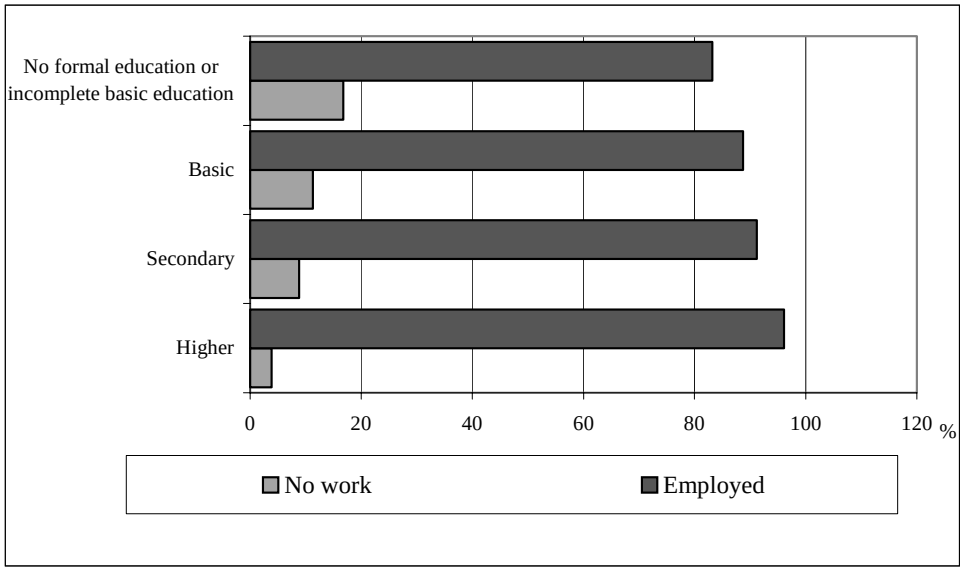
Figure 7. Job seekers by education level in rural areas in 1998 and 2002, %



Source: Central Statistical Bureau.

As Figure 8 shows, there is a positive correlation between employment and the level of education attained: an increase in education also increases employment prospects. There is also a negative correlation between unemployment and education: an increase in the level of education reduces the probability of unemployment.

Figure 8. Employment and unemployment levels by educational attainment in 2002, %



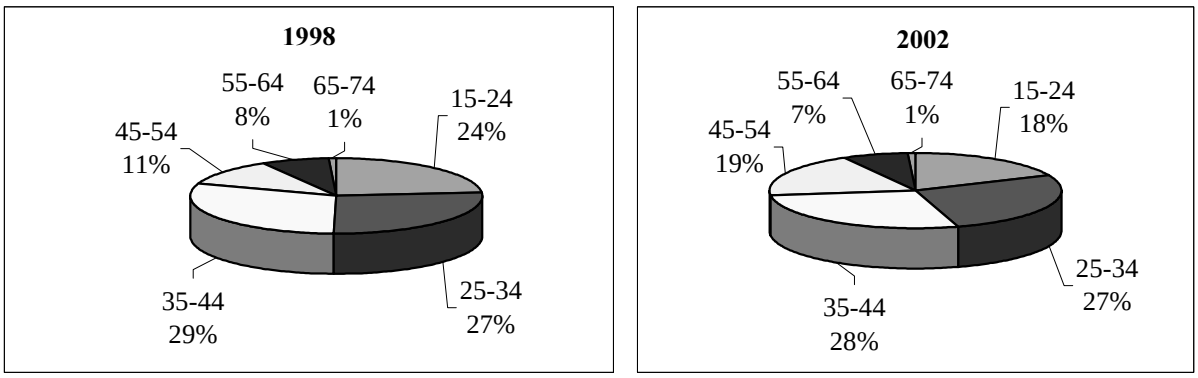
Source: Central Statistical Bureau.

Employment and age

Analysing the structure of unemployed in rural areas, the largest share of job seekers is in the 25-34 age group but if one compares this part of the population in 1998 and 2002, the share of young job seekers in the 25-34 age group is still the same. This could be due to a large share of the population in this age group.

Comparing changes in the number of job seekers in the 45 to 54 age group from 1998 to 2002, the share of job seekers in this age group has increased by 8%. This shows that this age group is the risk group, and it is difficult to find a job at this age.

Figure 9. Structure of job seekers by age in rural areas in 1998 and 2002, %



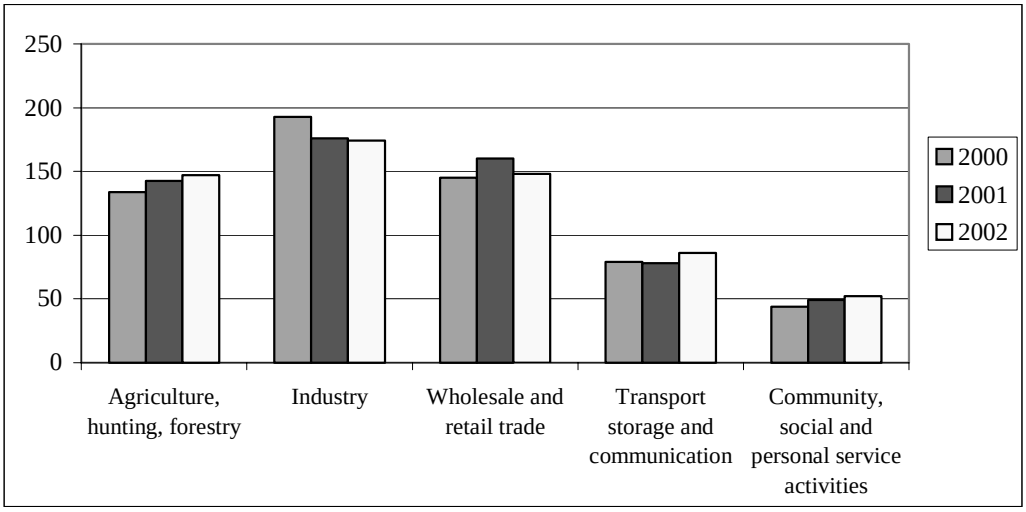
Source: Central Statistical Bureau.

Employment and sectors of the economy

The redistribution of employed among the sectors of the national economy in Latvia is continuing during the last five years, the number of people employed in agriculture and industry has decreased, while the number in construction and services has increased (Figure 10).

One of the reasons for the migration of employees between sectors could be the income level, for example, in some services the average monthly wage/salary is higher than the average wage/salary in the whole economy. Another reason is linked to the development of sectors; for example, the construction sector is linked with investment, which in turn influences the development of the construction sector.

Figure 10. Number employed in the main sectors of the economy in 2000–2002, '000



Source: Central Statistical Bureau.

Employment and rural, regional development

There is a significant relation between rural and regional development and the level of employment. As described above, the situation in the labour market is dependent on regional development. Insufficient provision of qualitative infrastructure, low entrepreneurial activity, low level of incomes, high proportion of low value added production in the economy and a high demographic burden all influence the employment level in a region. Therefore, local governments should concentrate more on regional development, fostering economic activities and providing conditions for the development of entrepreneurship.

Objectives of employment

In Latvia, the objectives of employment policy are fixed in several state documents, and one of them is the Declaration on the Intended Activities of the Cabinet of Ministers, which should be fulfilled in the lifetime of the government. Usually, the government acts for a four-year period.

The current government, formed at the end of 2002, has defined several objectives for employment development, and these are set in several sectors, including education, labour policy, social security and agriculture policies. For example, the following objectives are set in labour policy:

- Fostering the role of education in the society and wider preparation of new specialists in compliance with the needs of the Latvian economy.
- Support to state-level and private training and consultancy systems, which would form the basis for education of businesspersons and the enhancement of labour force qualifications.
- Reduction of unemployment paying special attention to the unemployment problems in different regions.

The government has fixed similar objectives in agriculture and rural development policies, including:

- Improving the long-term rural development strategy based on a balanced development of all types and all-size farms over Latvia, provision of new working places, diversification of the employment profile, etc.

And for social security policy the following objective has been defined:

- Provision of balanced development of the social and economic environment in the country, an increase in the number of working places, a reduction in unemployment, and a fostering of personal income.

And finally, the government has planned to implement an education policy, with the following objective: to provide an up-to-date, qualitative national education that complies with the requirements of the Latvian and global labour markets and meets the economic and social development needs of regions.

The objectives mentioned above show the importance of employment in the Latvian economy, and at the same time, emphasises that different sectoral policies should be coherent and targeted in the same direction, promoting balanced labour market development.

Besides the above mentioned policy targets, there are several strategic documents in Latvia. Signing the Treaty of Europe in Luxembourg in 1995, Latvia made a commitment to respect the EU requirements in the area of employment. The Concept of the Cabinet of Ministers "On Promotion of Employment" was adopted in 1999 and foresees the development of the National Employment Plan of Latvia, which has to be compatible with EU employment policy. The first National Employment Plan was developed in 2000. This Plan respects the goals of the employment policy for the year 2005 and 2010 put forward in the Lisbon and Stockholm EU summits and also the EU Council employment guidelines for 2002.

The Ministry of Economics, in co-operation with other ministries and social partners, has developed the National Employment Plan for 2003, putting emphasis on the development of measures, which might promote faster growth in employment and economic activity, the upheaval of quality and efficiency of work and the dynamic expansion of the labour market.

Instruments and efficiency of state policy

Active and passive measures of employment policy

The employment policy is an inseparable component of the national social and economic policy and is closely related to changes in the labour market. A correctly chosen approach to improvement will stimulate a more purposeful involvement of the working population into the labour market and also improve the adaptation of the labour force to the ongoing structural changes in the economy. The employment policy encompasses such areas as the establishment of the minimum salary, labour protection, and active participation in the labour market as well as labour relations.

Active employment measures offered by the State Employment Service are an important tool for raising competitiveness and employability. This is indicated by the fact that in 2001 more than two-thirds of the unemployed who participated in professional training succeeded in finding new jobs. The efficiency of this measure rose from 67.8% in 2001 to 79.8% in 2002. Still further adjustments of

all services, according to the needs in the labour market, are necessary. In this context it is very important to improve the administrative capacity of the State Employment Service by enhancing personnel skills and knowledge, improving the quality of the service, and developing work methods and the working environment.

In order to implement policy and reduce unemployment, the State Employment Service organizes and realizes the following active labour market measures:

- Vocational training and re-training of the unemployed.
- Paid temporary public works.
- Measures to increase competitiveness.
- Activities for disadvantaged groups [young unemployed of 15-25 years of age, unemployed with disabilities, unemployed after child care, pre-retirement age unemployed (less than 5 years left until the reaching of the age necessary for the granting of the State old age pension), long-term unemployed (more than 1 year), ex-offenders].
- Job-seekers' clubs.

According to Latvian legislation a passive measure is also provided, with compensation of income to a socially insured person in the event of unemployment.

The expenditure for active and passive measures for employment is showed in Table 5.

Table 5. The share of expenditures on employment measures as % of GDP from 1995 to 2002

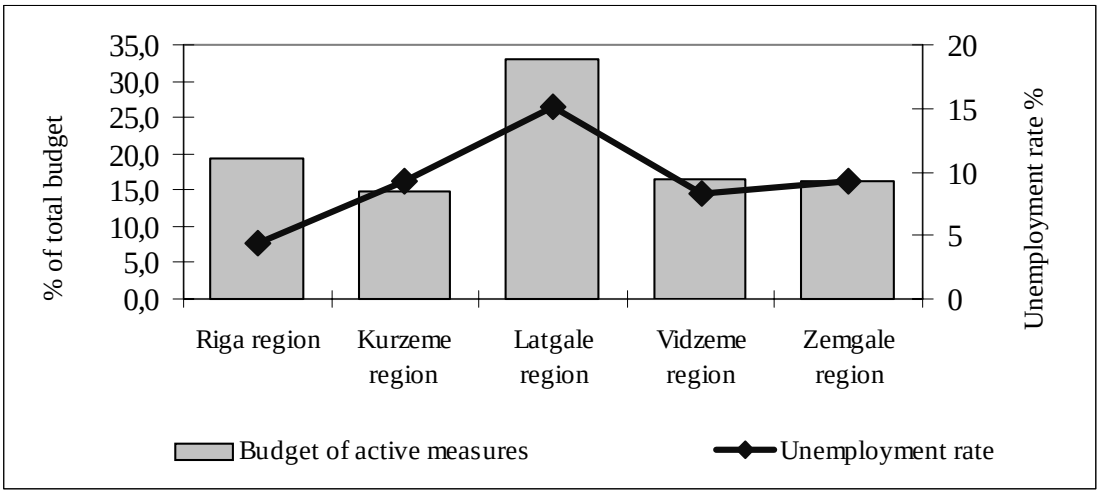
	1995	1996	1997	1998	1999	2000	2001	2002
Share of expenditures of active measures in GDP	0.15	0.13	0.11	0.19	0.21	0.16	0.15	0.09
Share of expenditures of passive measures in GDP	0.31	0.34	0.43	0.41	0.71	0.49	0.38	0.41
Share of total expenditures of employment in GDP	0.46	0.47	0.54	0.60	0.92	0.65	0.53	0.50

Source: Calculation is based on data of the Ministry of Agriculture and data of the Central Statistical Bureau.

The share of expenditures for employment in GDP measures has fallen since 2000, but in 1999 expenditures reached a peak – 0.92% of GDP, due to a significant increase in the registered employment. Table 5 shows that expenditures on passive measures went up in 1999.

Analysing the distribution of expenditures of active measures on a regional level, the highest share of expenditures for active measures has been spent in the Latgale region, which corresponds to the high unemployment rate in this region.

Figure 11. Finance of active measures and unemployment rate in 2002, %



Source: Central Statistical Bureau and the Employment State Service.

Fiscal policy

As explained in a previous chapter of this report, the high tax burden represents a significant barrier to the creation of jobs, at moderate wages, and a disincentive to the unemployed in searching for work. The government is planning to decrease the tax burden, which could promote employment activities in urban and rural regions of Latvia.

The government has in recent years also decreased the tax burden on businesses. This was basically achieved by a reduction in the rate of social insurance contributions. The legislation also provides for corporate income tax discounts, for instance, for large projects, enterprises producing high technology products and software, companies operating in special zones, and small enterprises. Starting in 2002, corporate income tax is reduced gradually from 25% to 15%. In 2002 it was 22%, 19% in 2003 and will be 15% in 2004. Since 2003, the rate of social contributions decreased from 35.09% to 33.09%.

Support of agriculture and rural development, and credit programmes

Credit programmes, which are aimed to extend or optimise production, or start new business activities that also promote the creation of new job places in Latvia are being implemented. For example, one of them is the "Agricultural Long-term Investment Credit Programme", which is mainly aimed at creating a long-term financing offer acceptable to agricultural holdings, expediting the attraction of investment for creation of farms of optimum size.

Another one is the "Non-agricultural Business Development Programme", which aims to facilitate economic development in rural areas by supporting non-agricultural businesses. The Programme grants loans and guarantees for businesses in case of insufficient loan guarantees.

These Programmes have been implemented recently and they could promote business activities and increase employment in the future.

The relevant support comes also from Foreign Financial Support for Rural, Agricultural and Forestry Development - SAPARD. The SAPARD programme has several measures, which are aimed at increasing the incomes of agricultural enterprises, the competitiveness and farming income, the competitiveness of the processing sector and its compliance to EU requirements. The objectives are to create employment and a more diverse employment structure in rural areas.

Conclusions

- The economic activity rate (participation in the labour market) in Latvia in 2002 was about 62% in the 15-74 age group. In rural areas, the economically active population comprise 59.3% of the total rural population.

- The number employed in agriculture, hunting and forestry has increased slightly. This is a positive tendency and employment has also increased in the overall economy.

- The number employed in rural areas increased since 2001, which shows that the economically active persons in rural areas have the possibility to be employed in other sectors, other then in agriculture.

- The largest share employed in agriculture, of total employment in rural areas, is in the Latgale region. In this region, almost half of those employed is involved in agricultural activities and agriculture is the main source of income for many households in the region. The possibilities for other types of activities are still limited in this region.

- A significant share of the population employed in agriculture is in the 55-74 age group; in 1998, it was about 25% of the total number employed in agriculture and in 2002 the share rose to 30%.

- Limited employment opportunities in other sectors is contributing to the outflow of the economically active, higher qualified rural population and youth to the bigger towns of Latvia. This accelerates the ageing of the rural population.

- The highest share of long-term unemployed was registered in several districts of the Latgale region, where the share was more than 50% of registered unemployed. A large proportion of long-term unemployed was in the 50 to 54 age group.

- The policy objectives defined by the current government emphasise that different sectoral policies should be coherent and targeted in the same direction, promoting balanced labour market developments.

- The share of expenditures for employment in GDP measures has fallen since 2000, but in 1999 expenditures reached a peak at 0.92% of GDP, due to a significant increase in the registered employment rate.

- The government is planning to lower the tax burden, which could promote employment activities in urban and rural regions of Latvia. Starting in 2002, corporate income tax is being reduced gradually from 25% to 15%. In 2002 it was 22%, 19% in 2003, and will be 15% in 2004.

- Relevant support also comes from the Foreign Financial Support for Rural, Agricultural and Forestry Development - SAPARD, which includes several measures to create employment and develop more diverse employment structures in rural areas.

- Credit programmes are also used as effective instruments to increase employment. These programmes are aimed at extending or optimising agricultural production, or starting new business activities and promoting the creation of new jobs in Latvia.

ANNEX 1: GLOSSARY

1) **Employed persons in agriculture, hunting and forestry or employed persons in agriculture** - employed persons accordingly section A or A01, of the NACE Rev. 1.1 Statistical Classification of Economic Activities in the European Community.

2) **Economically active population** consists of employed persons and non-working persons actively seeking a job (both those who are registered with the State Employment Board and those who are not).

3) **Population employed** (until 2001) refers to persons aged 15 years and over that during the reference week did any work for cash payment or compensation in goods or services. Self-employed persons with a business, farm or those who are undergoing professional practice are also considered as employed. Conscripts in the military service, whom in the reference week did some work for pay or profit are not considered as employed. Persons who are in temporary absence from work due to maternity leave or childcare leave of up to 3 months duration are classified as employed if, after the end of their leave, their return to the previous work is guaranteed. According to the ILO definition, the number of employed persons also includes those who work for own consumption and their work is an important source of livelihood for the person or the family.

   In 2002 – persons (aged 15-74) who during the reference week did any work for cash payment in goods or services, for at least one hour, whether payment was received in the week the work was done or not. Self employed persons with business, farm or professional practice are also considered to be employed if one of the following applies: the person works for the purpose of earning a profit, even if the enterprise is failing to make a profit (now); the person spends time on the operation of a business, professional practice or farm even if no sales are made (now), no professional service are rendered or nothing is actually produced; the person is in process setting up a business, farm or professional practice (buying or installing equipment, ordering supplies while preparing the opening of a new business).

   Persons who are in temporary absence from work due to maternity leave or childcare leave of up to 3 months duration are classified as employed if after the end of the leave their return to the previous work is guaranteed.

4) **Full time workers –** persons who usually work at least 40 hours per week.

5) **Part-time workers** – persons who usually work less than 40 hours per week, excluding those who consider themselves to be employed full-time irrespective of the number of working hours.

6) **Underemployment:** Until 2001 this indicator was expressed as the number of persons who would like to work regular hours, but who generally (and no by the choice, but by force) work shorter time than regular hours: persons, who are forced to work shorter hours; persons

who usually work regular hours, but during the reference week were forced to work shorter hours.

Since 2002, indicator is expressed as the number of persons who are forced to work part-time due to different reasons, who worked part-time, and who were looking for the possibility to work, or who would be ready to start additional work in two weeks.

7) **The unemployment rate** – the percentage share of persons registered with the State Employment Board and holding the status of unemployed in the total number of economically active population at the end of the period.

8) **Unemployed** is a non-working citizen or non-citizen of the Republic of Latvia or a foreigner (without any citizenship) who has received a licence for permanent stay, is of working age, able to work, is not engaged in entrepreneurial activities, is looking for work and is registered with the State Employment Board and applies to it at least once a month.

   According to the "Law on support to the unemployed persons and job seekers" that became effective on 1 July 2002 the status of unemployment can be granted also to a person who has received a permit for a temporary stay, is the spouse of the citizen or non-citizen of the Republic of Latvia or a person who has received a permit for a permanent stay in Latvia.

   Since the beginning of 2002, the unemployment rate has been changed making use of economically active population aged 15 years up to the retirement age obtained during the labour force survey. Formerly, it was the number of economically active with population aged 15 years and over.

9) **Job seekers** (both registered and non-registered with the State Employment Board) are persons who do not work and are not temporarily absent from work, are actively seeking a job and immediately available for work, if they find it.

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RECENT CHANGES IN RURAL LABOUR MARKET AND SOLUTIONS FOR INTEGRATING UNEMPLOYED INTO EMPLOYMENT IN LITHUANIA

By Mr. Martynas Storasta

Abstract

This paper analyses the current situation in the Lithuanian labour market in rural areas and describes possible ways to mitigate social consequences arising in that field. More detailed information is provided about the employment and demographic structure of rural regions. In the section on labour supply and demand analysis, this paper concentrates on professional qualifications and skills of the unemployed, and reviews the most recent trends in rural labour market statistics. Integrating policy principles are reviewed and presented in the next section of the paper. Several conclusions are drawn about the most suitable ways and methods to solve the problems of labour mobility and integration. The involvement of more relevant actors and the implementation of measures, which have been foreseen in the strategic documents, are highlighted.

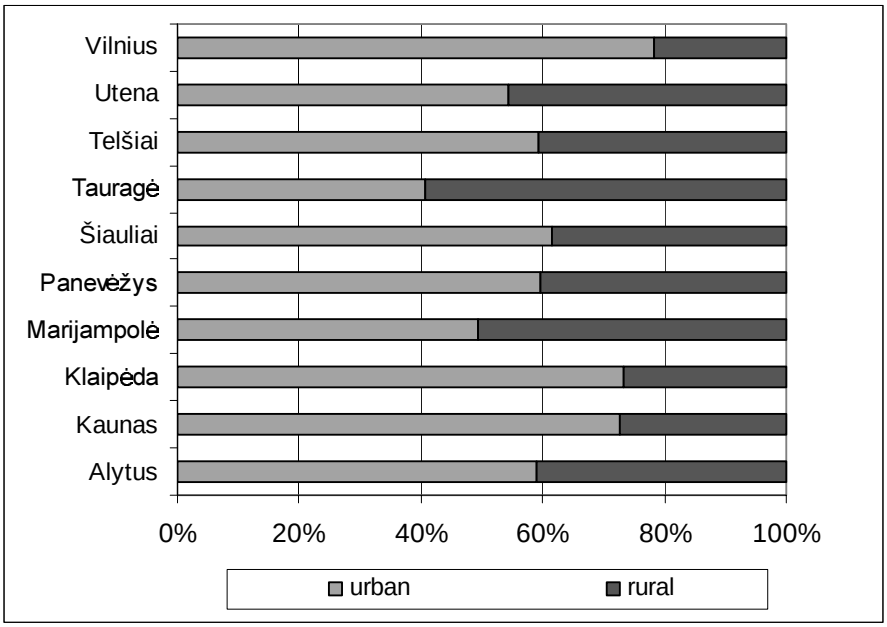
Introduction

Labour force mobility between urban and rural areas plays an important role in matching labour supply and demand. In general, it can be divided into several components, *i.e.* unemployment rate and its structure, employment structure and the demographic situation in the country. The need for higher labour force mobility may be explained as a need for complementary measures, which may help to reduce current territorial inequalities in employment and unemployment rates. Therefore, the main concept of this paper is to describe the variables, which have the most influence on labour markets and labour mobility in Lithuania.

General economic and demographic situation

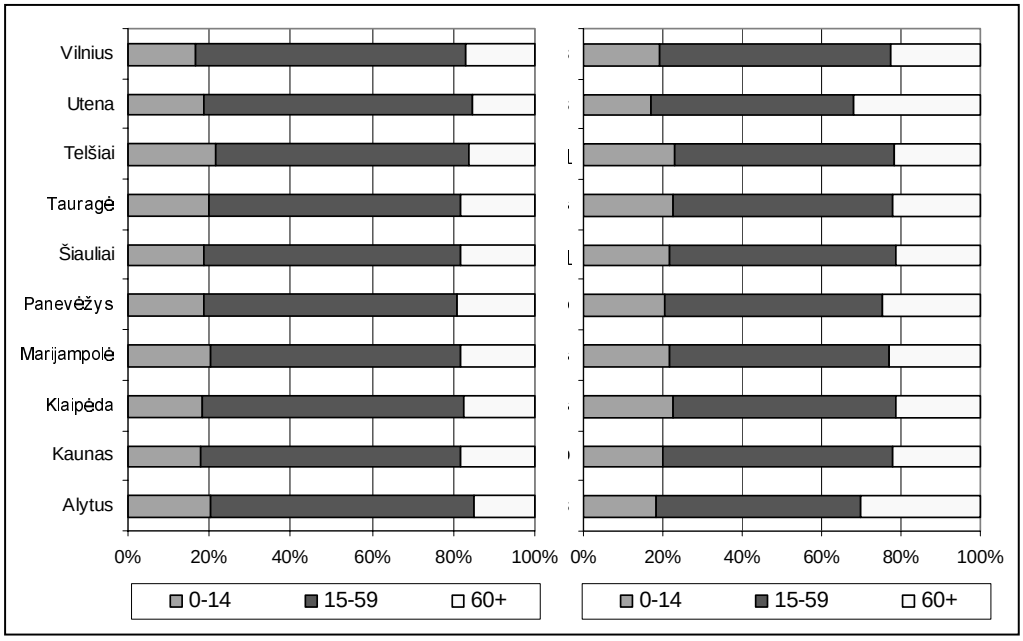
At the beginning of 2002 about two thirds of the population (66.9%) were living in urban areas. But, there were six counties in which the share of the rural population was larger than 40% (Chart 1).

Chart 1. Distribution of urban and rural population across counties in Lithuania



Source: Population of Lithuania 2001-2002, Department of Statistics of Lithuania, 2002.

Chart 2. Distribution of urban (left) and rural (right) population by age groups



Source: Population of Lithuania 2001-2002, Department of Statistics of Lithuania, 2002.

The largest share of the urban population live in Vilnius, Kaunas and Klaipėda counties, where the largest cities are situated. Most of the rural population is settled in Utena, Marijampolė and Tauragė counties.

The structure of the population by age group is almost the same in urban and rural areas. The only difference may be observed in the group of elderly people over 60 years (Chart 2). In all counties the urban population in this group is less than 20%, while in rural areas it is bigger, especially in Alytus and Utena counties, where it reaches almost 30%.

From the following data for 1989 and 2001 (Table 1) an interesting implication may be drawn. In the twelve-year period, the percentage of the working age population was growing both in urban and rural areas, whereas the share of the pension age population increased only in the urban areas. Another observation is more upsetting; a decrease in the total population as indicated by the diminishing number in the working age group. Therefore, the percentage of working age population seems to be growing.

Table 1. Breakdown of population by age group (pre-working age group excluded)

	1989			2001		
	Total	Urban	Rural	Total	Urban	Rural
	Thous					
Working age population	2 092.3	1 493.1	599.2	2 043.8	1 435.8	607.9
Pension age population	696.3	384.1	312.1	700.4	419.7	280.7
	in per cent					
Working age population	56.9	60.0	50.4	58.6	61.5	52.7
Pension age population	19.0	15.5	26.3	20.1	18.0	24.3

Source: Population of Lithuania 2001-2002, Department of Statistics of Lithuania, 2002.

The distribution of the population between urban and rural areas reflects the situation in gross domestic product per capita in counties. From Table 2 we can see that the lowest share of GDP occurs in the same three counties with the highest share of rural population. The large share of investments come to these regions and increases in production result in higher GDP per capita in Vilnius and Klaipėda counties.

Table 2. GDP per capita in different counties of Lithuania in 2001

	Thous. Lt	Compared to an average value, %
Total	13.8	100
Alytus	10.6	77.2
Kaunas	13.4	97.1
Klaipėda	15.1	109.5
Marijampolė	9.3	67.8
Panevėžys	11.8	85.3
Šiauliai	9.8	71.5
Tauragė	7.7	56.2
Telšiai	12	87.3
Utena	11.4	82.4
Vilnius	19.5	141.3

Source: Counties of Lithuania, Department of Statistics of Lithuania, 2003.

Employment situation in rural areas

The restructuring of the Lithuanian economy, market development, other internal and external factors have influenced changes in employment of the rural population. In 1993, the largest share of those employed were working in the agricultural sector. From this point of view, agriculture was the dominant branch of the economy. Starting in 1996 the share employed in this sector fell more rapidly; during the four-year period 1997-2001, it decreased by 36%. This reveals possible consequences of the processes related to the integration, which are witnessed in many EU member countries.

Table 3. Dynamics of the unemployed in agriculture (average annual data, '000)

	1991	1993	1995	1997	1999	2001
Agriculture	332.1	384.3	375.6	348.0	316.0	245.4

Source: Labour Market and Employment of Population, Department of Statistics of Lithuania, 1997, 2002.

This fall in employment in agriculture may be considered a positive change, and is led by the restructuring and modernising of the agricultural sector.

The number employed in rural areas fell by 23% in the period 1999-2001, and their activity rate by 8%. At the same time, the employment rate of those living in urban areas was almost stable; it has diminished by 1.3%. Unemployment in rural areas increased by 60%, while in urban areas it rose by about 9%.

Table 4. Employment, activity rate of the population and unemployment in rural areas (average annual figures)

	1999	2000	2001
Employed, thous.	540.6	510.0	416.6
Activity rate, per cent	57.0	56.0	52.5
Unemployment, per cent	9.0	12.8	14.4

Source: Labour Market and Employment of Population, Department of Statistics of Lithuania, 2002.

In 2001, the largest share of the labour force in rural areas worked in agriculture (50.7%) and services (34.6%). More than 88% of rural inhabitants were employed in agriculture.

The number employed in rural areas fell in agriculture, industry and construction, healthcare and social sectors. The increase in overall employment in small and medium-sized enterprises (SMEs), in wholesale and retail trade, services and governmental sectors did not compensate for the decrease.

Insufficient competitiveness of agriculture and the lack of ability to adopt to working in the market economy has driven many enterprises into bankruptcy. The increase in some sectors of industry and services are developed mostly in urban areas, where one may get good infrastructure and a skilled labour force. In rural areas, on the contrary, there is very little development in the service sector. Conditions for investment and possibilities to choose alternative branches of economic activity are very similar to those in urban areas.

The rural population has a low level of education and vocational skills to get a better job. Only 33.9% had high or higher education level (country average – 49.4%). Almost half of all rural inhabitants – 44% – were unskilled (country average – 29.8%). Counting those who have primary or lower level of education amounted to 69.4% of the rural population, primary education without vocational training – 57.2%.

Characteristics of job seekers from rural areas

The data analysis was done according to the labour supply data and a survey of 9 800 respondents from rural areas about their motivation and long-term unemployment situation.

The number of unemployed from rural areas has remained quite stable in recent years. In the 1999-2002 period, each month 7 000-7 500 unemployed persons were registered. Almost 2/3 of these were males (59.7%). The biggest growth was observed in the age group, over 50 years, it has increased by 2.7% percentage points (up to 16.5%). Low skilled and unskilled people predominate the structure of rural unemployed – only 2.5% have higher education. The largest share of these was without professional training, about 40%, 33.2% had primary education with professional or secondary education.

The number of unemployed searching for jobs for the first time has been increasing. In 2001 it reached 11% (2.5% more than in 1999). This means that one out of every ten unemployed persons was not employed before he or she was registered in the labour exchange. There is a constantly growing number of persons, who had worked in services before they registered. During 1999-2001, it increased by 5 percentage points, up to 35%. The largest share of unskilled unemployed was registered in Alytus, Utena and Kaunas counties.

On the whole, unemployed in rural areas are mostly elderly people, having no vocational training and those, who had no job for more than a year. This group of unemployed has comparatively low

motivation for work. According to a recent survey, one fourth of them (25.4%) registered with the purpose to get a note for social benefits and 49.1 to get a job. The distribution of urban unemployed was 13.3 and 78.1%, respectively.

Table 5. Structure of unemployed from rural areas, '000

	1999	2000	2001
Number of registered unemployed	82.5	92.8	89.1
By gender:			
-Men	46.9	53.5	52.1
-Women	35.6	39.3	37.0
By age groups:			
-Up to 24	18.9	21.5	20.1
-Over 50	11.4	14.1	14.2
By education level:			
-Higher	2.0	2.4	2.2
-High	11.4	12.9	12.8
-Other with vocational training	35.3	38.8	39.7
-Without vocational training	33.8	38.7	34.4
By earlier activity:			
-Unemployed	7.0	9.5	9.6
-Employed, out of them:	75.5	83.3	79.5
-Agriculture, forestry and fishery	28.6	27.9	24.6
-Industry	13.6	16.0	15.5
-Construction	9.4	9.9	8.6
-Services	23.9	29.5	30.8

Source: Lithuanian Labour Exchange.

Low work motivation and insufficient skills led to the rise in rural unemployment. The number of unemployed increased by 42.3% in a two-year period. The most rapid growth was witnessed in long term unemployment, which increased by 18.8 percentage points (up to 32.7%). Of this number, 34.9% were unemployed for more than 2 years.

Within the age structure the more notable changes took place in the age group over 50 years *i.e.* an increase of 4.9 percentage points (up to 16.5%).

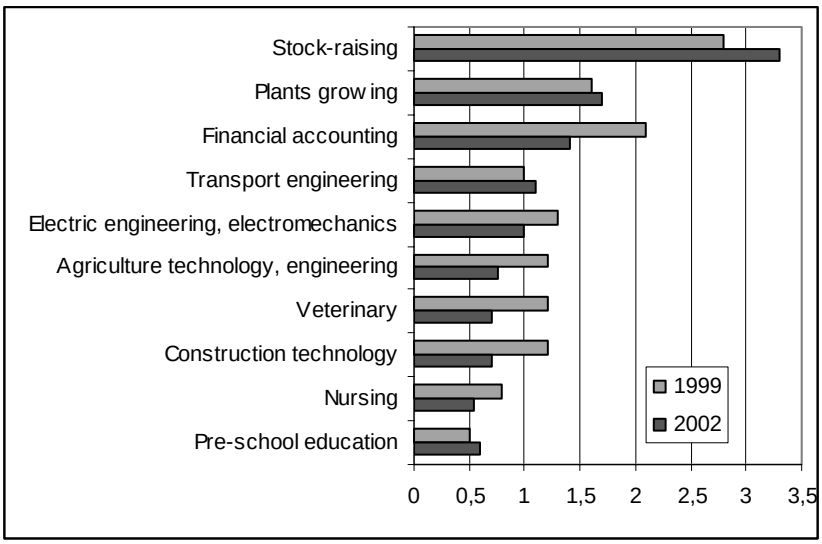
Similar growth was witnessed in the educational structure of the unemployed: the share of unskilled increased by 3.1 percentage points (up to 42.6%).

Table 6. Structure of unemployed in rural areas, '000

	2000-01-01	2001-01-01	2002-01-01
Number of registered unemployed	62.7	88.1	89.2
By gender:			
-Men	36.4	50.1	50.2
-Women	26.3	38.0	39.0
By age groups:			
-Up to 24	11.4	14.0	11.8
-Over 50	10.4	17.1	19.2
By educational level:			
-Having education and profession	37.9	50.8	51.0
-Without profession	24.8	37.3	38.2
By unemployment duration:			
-Over 12 months	8.7	23.4	29.2
Out of them – over 24 months	2.0	4.6	9.3

Source: Lithuanian Labour Exchange.

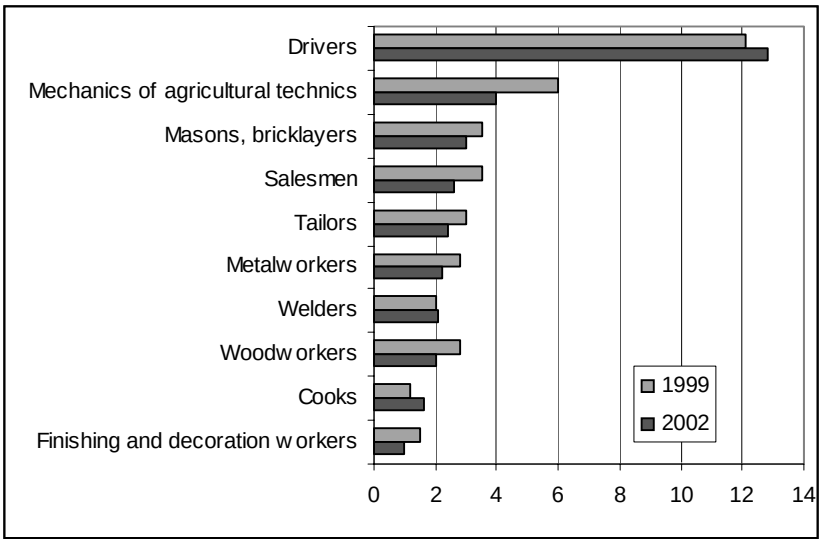
Chart 3. Top ten qualifications of unemployed, registered in rural areas (having high or higher education), '000



During the 1999-2002 period, the supply of specialists having high or higher level of education increased in the following groups: stockbreeders, growers, pre-school education, transport engineering, technical support and assistance.

Among skilled workers, most of the unemployed had qualifications as drivers, metal cutters, welders and cooks.

Chart 4. Top ten qualifications of the unemployed, registered in rural areas (having secondary, compulsory or primary education), '000



Characteristics of labour demand in rural areas

The analysis of labour demand and structural changes refers to a survey of employers and statistical data of labour demand. The latter survey covered about 1 300 employers, who created jobs in rural areas.

Table 7. Structure of labour demand in rural areas, thous.

	1999	2000	2001
Registered number of vacancies	26.5	28.9	31.8
By type of agreement:			
-Permanent jobs	19.9	19.4	21.6
-Temporary jobs	6.5	9.5	10.2
By economic activity:			
-Agriculture, forestry and fishery	17.5	17.2	17.2
-Industry	2.4	3.1	3.1
-Construction	1.2	1.2	1.0
-Services	5.4	7.5	10.5
By education level:			
-Higher	1.6	1.8	2.4
-High	7.2	7.7	7.9
-Other with vocational training	6.0	8.0	10.2
-Without vocational training	11.7	11.4	11.3

Source: Lithuanian Labour Exchange.

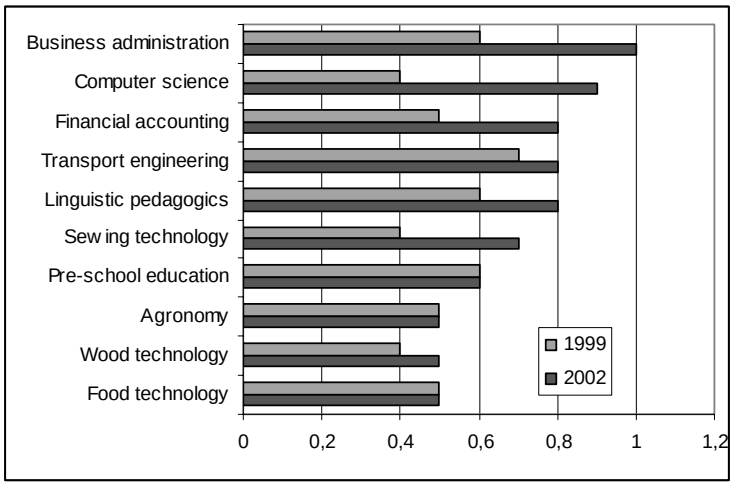
In the 1999-2002 period, labour demand in rural areas increased by one-third, while in urban areas it doubled. Employers in rural areas opened more temporary jobs. Therefore, the biggest growth of demand was observed in temporary jobs, which increased by 7.8 percentage points (up to 32.3%).

Within the main sectors of the economy, demand grew most in the service sector, which expanded by 15.9% (up to 36.3%). Still the largest demand remains in the agriculture sector; 49.7% of all jobs.

Employers from rural areas started to pay more attention to professional qualifications of their workers. As proof of this, demand in the sector for those having education and vocational training increased by 15 percentage points, up to 70.9%.

In urban areas, on the contrary, a much larger share of labour demand was for permanent jobs. The portion of free vacancies in services and the construction sectors are also larger than in rural areas. Urban employers have more vacancies for workers who have higher education.

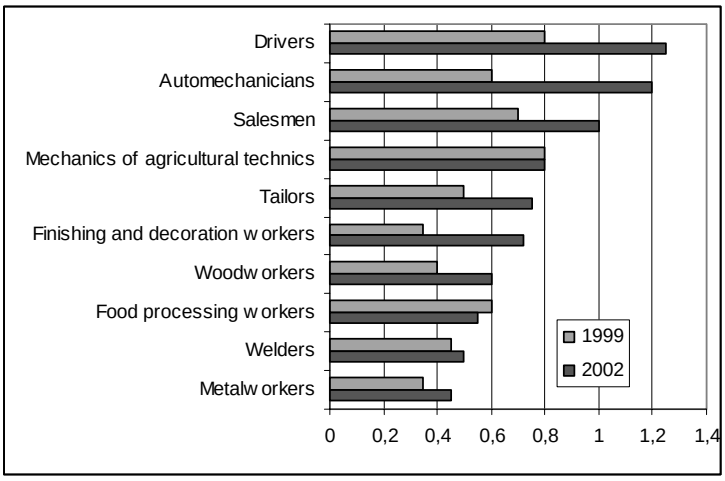
Chart 5. Demand for specialists with high or higher education levels, '000



Employers set the highest qualification requirements for new employees from Vilnius, Klaipėda, Šiauliai and Telšiai counties. Moreover, requirements for personal characteristics of workers increased.

The overall tendency in the Lithuanian labour market show an increasing demand for highly skilled specialists and workers. Demand is constantly growing in light industry, woodenware, and consumer goods production sectors, while the lowest demand for labour is in agriculture.

Chart 6. Demand for workers with primary or secondary education levels, '000



Meanwhile, low qualifications and unskilled labour are less marketable, the majority of rural inhabitants has inadequate education, insufficient vocational training and personal skills. The latter attributes do not match the rising requirements of an evolving market economy.

In order to overcome such a mismatch there is a need for a highly developed system of vocational training, which should be available for everyone.

Labour demand for professionals has changed a lot in rural areas during the period 1999-2002. Demand grew rapidly for specialists in management, business administration, and languages, accounting, sewing and the technology fields. A higher demand for workers was witnessed in sectors such as finishing and decoration, car maintenance, services and sales. Most of the demand for workers is now shifting from agriculture to management, business, IT and the advertising sector.

Development of procedures to integrate rural unemployed into the labour market

Many people from rural areas lack initiative, computer literacy, knowledge of foreign languages, communication skills, all of these have the common name "new major skills". Almost half of the unemployed from rural areas have no vocational readiness; among these there are lots of people having only basic or primary education. In developing a market economy Lithuania needs to have more competitive human capital, which on the whole, is determined by growing employment and a highly skilled labour force.

The Ministry of Science and Education and The Lithuanian Labour Exchange have to join forces to create a common database of registered vacancies, learning possibilities and other information relevant for better education of the population. This might give more possibilities to get up-to-date information about labour demand, vocational training, etc. It could also increase geographic and intersectional mobility of labour and help to raise the level of qualifications.

The Lithuanian Labour Exchange provides great attention to match labour supply and demand. This process involves the realisation of labour market policy programmes, preparation of specific programmes like projects of local initiatives, first step in the labour market, bank of talents, unemployment prevention, vocational training of young unemployed, active integration of graduates from high and higher schools. There are also other services provided, which are based on information

systems development; open information and counselling systems. Most of these services are now available through the Internet.

While implementing the programme of Reduction of unemployment in 2001, the Lithuanian Labour Exchange began the implementation process of the local initiative projects. Such projects are aimed at the activation of local communities by increasing employment in the areas with the highest unemployment. These projects actually help to create more new workplaces on the basis of partnerships and help to solve social problems associated with high unemployment. Locally based employers get financial support to create new workplaces in particular areas.

The results of these projects are really optimistic, as during the two-year period (2001-2002) there were 530 new job places created. Projects conducted in rural areas have created about 140 new job places. They are aimed mostly at vegetable, production intensive stock raising and other activities.

According to the research executed by the Institute of social research and labour, households of long term unemployed in rural areas are not homogeneous according to their income rate. A majority of them is ranked at the lowest social layer.

People who have no job for a long time lose their skills, readiness to work, and economic and social behaviour. They become less self-confident, so there is a need to have more complex and sophisticated measures to integrate them into the labour market. One example could be the organisation of some additional measures for unemployment prevention, by encouraging employers to employ such persons.

Other programmes and strategies are created and pursued besides those mentioned above. These include the “Medium-term strategy for the Lithuanian economy within the framework of integration into the EU”, “Strategic guidelines for the development of small and medium enterprises until 2003”, “Agriculture and rural areas growth strategy”, “National programme for tourism development” and many others. These documents include statements about increasing the number of vacancies in rural areas, raising the level of the economy, increasing employment of rural inhabitants, and creating new, alternative job places in rural areas. In the “Long-term strategy for Lithuanian economy development” there is a section on SWOT analysis, which says that the labour force in Lithuania is skilled enough, but at the same time, it has low mobility and low ability to adapt to the changes that arise in labour markets. As a consequence of this, there is a lack of skilled labour in some sectors, but nevertheless, unemployment is still high. On the other side, mobility of labour might lead to “brain drain”, which is not acceptable at this stage, where Lithuania is at the point of strong economic growth.

Conclusions and suggestions

As there is no recent comprehensive study on labour force mobility in Lithuania, as a first step, such a survey should be conducted. This survey should examine the structure of the economy and population in rural and urban areas.

At the second stage, some additional measures should be introduced to stimulate local community and enterprise development. These kind of activities in rural areas would lead to better and higher employment. Farmers should start alternative economic activities that may be consistent with landscape and environment (like ecological agriculture or country tourism).

Greater investment into social care should be encouraged. This will lead to a reduction in poverty in rural areas. On the other hand, it could mitigate the consequences of social exclusion.

More emphasis should be directed towards training courses for persons who start their own businesses. These measures might be helpful for regions with less developed business infrastructure, high unemployment rates, etc.

The integration of the unskilled, young, and long term unemployed will lead to a better and more balanced employment of the active population, and a more evenly distributed labour force in urban and rural areas.

The availability of training facilities and a higher quality of counselling services might lead to an increase in labour mobility across the regions.

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Session 2 Discussant Paper

By Dr. Waldemar Guba

The important concern today, in the eve of accession of the Baltic countries and several other CEEC to the EU, is how the EU membership will affect agricultural and rural employment in those countries and, in particular, whether it is going to favour labour mobility in rural areas and how? This is an aspect of the much broader debate on the prospects for benefits of economic integration, such as growth and job creation, as well as the impact of the CAP and structural funds.

Let's consider the relative income position of the farm sector – still the major employer in rural areas in most of these countries. The usually stipulated expectation is that increased subsidization due to the CAP will decrease the incentive to leave agriculture. This is true, however, several other offsetting factors will simultaneously be in place.

First, processes outside the sector, which are conducive to increasing the income gap.

- Accession is expected to sustain high rates of productivity and income growth in non-farm sectors.

- Increase in labour productivity in industrial sectors, coupled with the inflow of foreign capital (both private and budgetary transfers), may reinforce the tendency towards real appreciation of domestic currencies, thus deteriorating sectoral terms of trade in tradable sectors, including agriculture. This effects was very clear in recent years in Poland being the major factor of declining real farm incomes.

Second, increased production costs.

- Accession will impose rigid technological requirements related to statutory standards and to competition on the single market. This means a burden of high modernization costs. Only a part of these costs will be covered by subsidies under the rural development programmes.

Last, but not least, even a positive net effect on farm incomes might have rather moderate consequences for labour mobility given the magnitude of the initial productivity and income gap.

Accession may also bring less demand for labour in agriculture:

- Increased statutory standards, in particular, apply to those farm activities which tend to be more labour intensive (milk, livestock production). This induced technological change is both labour-saving (more capital intensive) and increases the minimum efficient scale of farm operation. The issue of adapting the capability of small farms is of greatest significance in countries with fragmented farm structures such as Lithuania and Poland.

- Only in the longer run can one expect a change in activity structure of the farm sector in line with the principle of comparative advantage *vis-à-vis* the enlarged single market towards those more labour intensive. Two considerations are of importance here: (i) The 'positive' (increasing) effect for labour demand may however be offset by employment of new technology vintages that tend to be labour saving, (ii) the production control measures of CAP (production and support quota) tend to constrain this opportunity since it focuses on

activities with comparative advantage in the new member states (milk, beef and to a degree fruit and vegetables).

What about the demand for labour outside agriculture?

- In the short term, accession may worsen the situation on the urban labour market which, in turn, may diminish opportunities to reduce rural unemployment. Inherently, economic integration is bound to induce large structural changes economy-wide and, in addition, force new member states to get rid of the structural imbalances inherited from the past. A temporary increase in structural unemployment is probable. In such circumstances improvement of competitiveness of rural and agricultural population in the labour market requires not only an improvement of their education, but faster improvement in relation to urban areas.

- In the long term, the observed tendency for high regional concentration of economic growth may persist. This tendency is reinforced by poor transportation infrastructure in the new member states. Coupled with the low propensity for interregional migration (observed in Poland) it is conducive to growing regional disparities in job creation and unemployment. Since the lagging regions tend to be mostly rural the regionalisation of growth may exacerbate the problem of farm and rural unemployment.

How promising is the rural development policy package offered by the Community? The rural part of the structural funds and the 2nd pillar of CAP may have an ambiguous effect on farm employment. The set of instruments within these programmes is relatively wide and provides for adjustment to specific needs. At the same time the rationale on which the original design of these instruments was based does not perfectly fit the major challenges of the agriculture and rural areas in the new member states. Importantly: (i) major instruments of support to the new job creation in rural areas are within other (non-farm) components of structural funds, (ii) the most promising instruments focusing on bottom-up initiatives need time to be developed, (iii) in the proposal for programming documents in Poland, for example, the major focus is on SAPARD-like approach, *i.e.* support to modernization and restructuring of the food economy. Such a focus is fully justified from an efficiency point of view, because modernization is necessary for these sectors to stay competitive on the single market. However, at the same time, it will promote concentration of production structures and reduction of employment in agriculture.

Summary

Accession is expected to cause an increase in the incentives to move from farming to other activities. This is because of the deterioration of the sectoral terms of trade related to the changing macro-relations. Only in the short term will this effect be mitigated by the CAP. In addition, technological change in the farm sector, which is being induced by the single market and the *acquis* requirements is expected to cause a decline in demand for farm labour. In turn, an increased demand for farm labour due to the output structure adjustment towards more labour intensive activities will have a rather small impact and will be fully revealed in the long term. Labour outflow from the farm sector is primarily conditioned by the demand for labour economy-wide. Structural adjustment due to accession may temporarily increase structural unemployment outside agriculture, however, much will depend on the soundness of the economic policy. A significant challenge comes from the mismatch between the regional location of the agricultural/rural unemployment and regional concentration of growth (and new jobs). Increased propensity (subjective factors) and possibilities (objective factors) to migrate to other regions are necessary in any case.

Session 2 Discussant Paper

By Dr. Tomas Ratinger

The three papers document the development of labour markets in the Baltic countries over the last five years. They illustrate that, although there are many similarities, given the same recent history, the problems differ in their magnitude. Let us first review the main observations from the papers referring to some features of the labour markets in the individual countries:

Estonia

- The paper reports significant regional differences, in particular, significant unemployment in the very industrial Northeast region.
- In rural regions labour has moved from agriculture to services – at least in relative terms.
- The participation rate has declined, but the number of inactive people has increased, especially the number of discouraged people.
- Persons who have worked in agriculture are likely to become inactive rather than registered as unemployed.
- The non-Estonian speaking population has found it more difficult to maintain or get a job.

Latvia

- The participation rate declined (except for Riga) during the last 5 years.
- There has been a dramatic decline in employment in agriculture (by 32% on average, 1998-2002).
- Shifts from agriculture to forestry have been noticed. In general, it can be (indirectly) assessed that people released from agriculture have been able to find jobs in other sectors.
- One third of employed people in rural areas are only in part-time jobs.
- Shedding of young people, particularly from agriculture is common in rural areas.
- Only two-thirds of unemployed people have registered.
- Most of the unemployed are persons with incomplete or basic education.
- However, there is a significant proportion of people with secondary education who have been laid off.
- Employment in agriculture, hunting and forestry is still comparable with the industry (24 and 28% respectively).

Lithuania

- The paper reports big regional differences in economic performance.
- There was a dramatic loss of jobs in rural areas (for rural population); agriculture contributed significantly, it released a third of its employees (inc. self employed) between 1997-2001.
- Also, the service sector has released a lot of people.
- The proportion of long-term unemployed and young (first time job seekers) people has grown.
- Problems assumed in the mismatch between education and skills offered and demanded (exception – drivers) in rural areas.

Common problems

A lack of human capital is regarded as the main obstacle for development of rural (as well as general) labour markets in all three Baltic countries. First of all, a low level of education of the rural labour force, but also a mismatch between offered and demanded skills. This fact causes people to stay unemployed for a long time, some of them having given up looking for a job. The number of discouraged peoples has risen in all three countries, however, the magnitude of this problem seems to be most severe in Lithuania.

Agriculture absorbed a lot of labour in Latvia and Lithuania in the first half of the 1990s. The situation has changed since 1998. Similar to Estonia (and other Central European Countries), agriculture significantly contracted in terms of labour employment. Farm restructuring and economies of scale, and particularly modernisation, has caused a loss of agricultural jobs. There will hardly be more agricultural jobs in the future, although farm income will improve after accession. This is an observation made in many countries with relatively cheap labour - that technological progress tends to exclude labour, because most of the new technologies are developed in countries with expensive labour and relatively cheap capital (Bailey, 2000).

Baltic rural areas are characterised by a low level of entrepreneurial activity; economic growth is usually concentrated close to the capital city and the surrounding area. It might be due to missing regional policies, but also due to high transaction cost and insufficient social capital, that rural people cannot build viable businesses.

Concerning labour mobility and its spatial dimension we can conclude that no significant migration has been observed. It might be because of high costs of moving, but also due to insufficient education, and a fear of losing family support. The latter can also be associated with ethnicity; the Russian population tend to stay in those regions where they dominate. On the other hand, we can see structural shifts, however, lack of skills prevent people from switching. Also infrastructure (*e.g.* public transport availability) might hamper finding jobs in other sectors.

Policies

The labour market problems in the Baltic countries are obviously associated with economic transition and accompanying economic decline. A lot of people were laid off because uncompetitive businesses collapsed in the 1990s. However, the Baltic economies have recovered since the EU accession talks and processes started. EU accession is regarded as a big challenge, but to utilise it,

appropriate policies are needed. Concerning the labour market, policies need to tackle three areas: incentives to the private sector, labour skill and education and support for the unemployed to find jobs.

Starting with the worst, unemployment offices failed to fulfil their role - to assist people to find a job. This significantly contributed to the figures of a declining participation rate. On the other hand, retraining improved significantly the chance to get a job for 70% of attendees, but the extent of these programmes was limited.

The governments of the Baltic countries stimulated job creation by giving incentives to the private sector either by tax holidays or even more directly by lowering the rate of social contribution (and thus lowering labour costs, Latvia).

It seems that the Baltics deployed the other policy options less, like support to development of agricultural and non-agricultural businesses (SME), by improving access to credits, investment grants, etc. combined with regional planning.

Diversification

In this context it might be useful to mention results from a study on farm diversification conducted in the framework of the IDARA (EU 5FP) project in the Czech Republic, Hungary and Poland (Chaplin, H, 2003). Our investigation concluded that:

- Basic infrastructure is critical, particularly the availability of public transport (in Poland and Hungary).

- There were differences between subsistence and commercial farming, subsistence farms topped up their income by off farm jobs, while commercial farms tended to utilise released factors in on-farm non-agricultural production.

- On-farm diversification depended on access to capital (not only interest rates, but issues like sound business plans, separate agricultural and non-agricultural funds, access to bank offices mattered).

We also found that on-farm diversification depended on informal networks which were not necessarily sustainable. Therefore, there is a need for regional development agencies, advisories, etc. which enable businesses to exchange information, find contractors and co-operate.

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SESSION 3. RURAL AND REGIONAL DEVELOPMENT POLICIES

DEVELOPING AN INTEGRATED POLICY FOR RURAL AND REGIONAL AREAS IN THE BALTIC COUNTRIES

By Dr. Helena Johansson and Dr. Ewa Rabinowicz
(Paper presented by Dr. H. Johansson)

Abstract

Recognising that market forces is an efficient mechanism for allocating scarce resources in a society, government intervention can only be justified when market forces, for some reason fail to generate an efficient market equilibrium, or when the market equilibrium is perceived to be "unfair" on equity grounds. This paper focuses primarily on the extent to which existing market failures hinder rural development, both in general terms and with special regard to the Baltic countries, and discusses whether existing policies are indeed addressing underlying malfunctions of the economy.

Introduction

Policies that promote integrated rural development instead of traditional agricultural policy measures have been advocated for a long time, see for instance Saraceno (2002) or Buckwell *et al.* (1997). At first, appeals of this type were contained to the academic quarters. However, it appears now that rural development issues have moved to the top of the political agenda in Europe. Modulation, *i.e.* transfer of funds from support of agricultural production to support of rural regions, which is one of the key elements of the midterm review (MTR) proposal of the European common agricultural policy (CAP), could be used as a case in point. Important to note here is that the focus, especially in the case of MTR, seems to be on *replacement* rather than on an examination of the needs for, or merits of, rural development policy *per se*, that is on more extensive use of existing instruments than on an unconditional search for appropriate ones. The issue of theoretical foundations of a rural policy regime requires a serious debate, if such a policy is intended to play a more important role in the future. The rationale for agricultural policies in the past, at least at the outset, was the "*specificity of agriculture*" *i.e.* the alleged inability of production factors engaged in farming to command a fair rate of return on an unregulated market.[1] A question that could be asked at this point is whether there is a "*specificity of rural regions*" which could justify rural policy? In what sense is rurality a problem or a handicap? Or, is it instead an asset?

Rural and regional policies are based on two underlying assumptions: that spontaneous development is unsatisfactory on some account, such as efficiency or equity, and it is possible to correct this development at reasonable costs. An understanding of the underlying economic processes that generate regional disparities is fundamental for the proper design of a policy that aims at producing a remedy. Hence, we will examine the prevalence of market failures, especially in transition economies. What kind of policy response could correction of those market failures require? A different way of looking at the same issue would be to ask whether compelling scientific arguments support the general principles inspiring current policies in the EU that aim at promoting rural development. Especially, what apparent market failures are addressed by existing policies? To what extent do existing policies match problems faced by rural regions? By comparing these two perspectives we attempt to arrive at recommendations about what rural development policies should, and should not, do - both in general terms and in relation to specific conditions in transition economies. The approach

1. Whether the traditional arguments for the specificity of agriculture are valid any longer, or ever were, is another matter. This issue will not be disputed here, see for example Molander (1993) for a discussion.

chosen may seem as a pure academic exercise. However, correcting non-existent market failures, while ignoring real ones is a bit like mending things that "aint broken", while overlooking true problems. Though, it shall be remembered that the existence of a market failure is a prerequisite, not a sufficient condition, for market intervention and further, that the means should be designed efficiently in case of intervention.

The outline of the paper is as follows. First, theoretical justifications of state intervention will be discussed. Second, existing policies will be shortly described and scrutinised looking for the underlying assumptions. This general discussion is next extended to problems faced by rural regions in the Baltic countries. It should be noted that this paper, in spite of its' ambitious title, can hardly offer specific advice on how to design rural development policies in each of the Baltic countries. The objective is more to raise some important, but neglected, issues rather than to solve them.[2]

The role of government

Observations of income disparities between urban and rural areas, high rural unemployment rates in combination with net migration from several rural areas have raised concerns among the public and policy makers, and have resulted in special assistance to stimulate rural development in order to reduce inequalities between regions. In addition to equity considerations, it is often argued that a reduction of regional disparities will raise the overall economic efficiency within the country. At the heart of the matter is the underlying process explaining the divergent regional development tracks, and a central question is whether the lack of regional convergence is caused by market failures. In order to clarify matters, economic theory offers help but there is, however, no single coherent theoretical framework explaining the regional development process. Instead, the combined insights from several theoretical fields yield a starting point from which the issue of potential market failures can be evaluated.

The neoclassical trade and growth models

According to the traditional neoclassical theories of trade, differences in production patterns and standards of living between countries, or between regions within a country, can be explained by the underlying attributes of the spatial area in terms of endowments of natural resources and factors of production, and the available technology. This type of models suggests that countries, or regions, will specialise in accordance with their comparative advantage based upon these given characteristics, and that this specialisation is favourable for both prosperous and poor regions. If the regions have similar endowments and technology, it is further suggested that mobility of factors of production and/or goods ensures that factor returns will be equalised, resulting in a convergence of income levels between regions. Similarly, the neoclassical growth models also predict convergence. Given that factors of production are mobile across regions, initial differences in wages and other factor returns will be eliminated when the factors move to the regions where the return is the highest. Extending the traditional growth model framework, the so called endogenous growth theory highlights the role of technology diffusion, that is the extent to which new technology tends to spread between firms, regions and countries. The underlying determinants of output growth are growth of labour and capital, in combination with technological progress. Intra-regional differences in income levels can hence be

2. The concept of integrated rural development embodies a principle of involvement, *i.e.* the active participation of local communities in the process of policy formulation and delivery. Several issues connect to the question of local participation, for instance the choice of a proper balance between bottom-up and top-down approaches in policy making, (Baldlock *et al.*, 2001). This paper will, however, focus only on economic justifications of rural development policies, and not discuss issues related to policy delivery and administration.

the consequence of insufficient technology diffusion between regions, region specific obstacles to investment and differences in labour force growth. In addition, if labour mobility is constrained, regional differences can persist.

Although an important contribution to our understanding of regional development processes, these models alone cannot, however, account for the observed far-reaching spatial concentration of economic activities and the pervasiveness of inequalities in income levels and growth rates between regions. Instead, the more recent models of *e.g.* "new geography" indicate that the present situation is the result of an interaction between concentration and dispersion forces, where concentration gives rise to economic advantages but also creates inequalities between regions.

The "new geography" models

The classical models of spatial economics rest upon three key variables; economies of scale, transport costs and competition for scarce resources in the centre. If there were no fixed costs or increasing returns of some sort, factories would subdivide to be close to each consumer. Increasing return can be either external or internal to the firm. Internal economies of scale means that the cost per unit decreases with the volume of production, while external economies of scale occur when firms achieve cost savings when operating in the context of a larger local economy. Such savings can arise from localised knowledge spillovers, access to diversified inputs or specialised services, or externalities in the labour markets. Those knowledge spillovers can be due to a sharing of ideas among firms through the movement of workers across firms or learning/observing between neighbouring firms. There are also gains from location, where an already trained supply of skilled workers exist, making it easier to match workers' skills and job requirements. Strong labour markets, moreover, also insure workers against firm and industry specific shocks. In addition, there are agglomeration benefits in consumption as well, because of the higher variety of consumer goods available in larger agglomerations. Altogether, those advantages make agglomeration favourable for individuals in their role as labour, producers or consumers, and therefore, economic activity tends to concentrate in space. In contrast, there are also dispersion forces counteracting agglomeration. For instance, competition for land and other immobile factors will emerge in the central places, driving up prices. Other dispersion forces are negative externalities from congestion such as increased costs of living, long distance commuting, pollution, crime and anonymity.

The ongoing development in Europe can be understood in terms of these counteracting forces. A disperse pattern of settlements was natural in a low-income, high transport cost economy dominated by agriculture, which is a land dependent sector with relatively low scale economies. Rapid technological change, combined with a decreasing share of income spent on food, resulted in a falling demand for labour in this sector. Instead, labour tended to move to activities characterised by greater economies of scale, both internal and external, that is with agglomeration advantages. An increased share of spending on non-agricultural goods contributed likewise to a desire of households to move to cities where a larger variety of goods are available. The result was a persistent rural out-migration, in particular, from peripheral regions. However, in some rural areas a shift in the urban/rural migration pattern occurred in the 1970s. Migration toward the centres was replaced by net migration toward peri-urban and rural areas. Dispersion forces which have contributed to this change included diseconomies of agglomeration like congestion, a preference for home-ownership and a growing demand for space and for certain rural amenities. Further, the commuting zones had widened due to improved traffic facilities, permitting people to live in rural areas and commute to nearby towns. As a result, the structure of many rural areas is now similar to that of urban areas, and non-agricultural employment dominates. Moreover, in several countries dynamic rural regions, although not a majority, perform better than the more urbanised, but lagging regions. According to Saraceno (2002), the number of rural areas attracting population exceeds that of rural areas loosing population, and

OECD (1996) has shown that new employment opportunities have not been correlated with the degree of rurality.

The potential efficiency gains from agglomeration means that policies counteracting agglomeration can come at a cost, because of a trade-off between the overall national growth rate and the degree of regional inequalities (Martin, 1998). It is also shown that strong economic forces drive concentration, meaning that it can be difficult to reverse the current trend, even if one is prepared to pay the costs. Hence, the direction of rural policy comes into focus, as well as the relation between urban and rural areas. For instance, low-density agglomerations may offer many of the economic advantages of agglomeration, while also reducing the costs of congestion in the large agglomerations. In Norway, for example, regional policy has intended to stimulate urban centres in rural areas, hoping that local agglomerations have a beneficial impact on the surrounding rural areas (Polèse *et al.*, 2002). Finally, infrastructure subsidies, which would make peripheral regions less peripheral, are often advocated as relatively efficient, non-distorting ways to help underdeveloped regions. However, it is not certain that the improvement of transport infrastructure that lowers transport costs, facilitates convergence. Instead, the "new geography" model suggests that the actual long term effect could be the reverse, since lowered transport cost facilitates the concentration of production. This is conducive to overall national efficiency and growth, but enhances regional inequalities.

What kind of market failures can be found in rural areas?

Two types of market failures that potentially can hinder rural development can be identified. First, "traditional" market failures that can exist in all locations, but for some reason are exacerbated by rurality, and second, market failures that are due to rurality in some way, meaning that the introduction of space and distance creates its own market failures. It is also possible that several market failures in rural areas reinforce each other, thereby creating negative synergies.

Traditional market failures identified in economic theory are lack of competition, information failures, the presence of external effects and public goods, and incomplete markets, especially in the case of insurance and loans. For rural areas, it has been suggested that market failures associated with the insurance and capital markets could be more frequent and severe than in urban areas (de Janvry and Sadoulet, 2002). For instance, farmers and other small-scale rural entrepreneurs could, more often, be rejected when searching for finance in the private market, than a comparable firm located in the urban area with a similar risk profile, because of an information gap (Fleisher and Felsenstein, 2000). As indicated by traditional growth theory, too slow capital growth has a negative impact on economic growth.

The second class of market failure concerns potential non-optimal outcomes in the pattern of economic geography that is induced by market forces. In this context, the question is whether market forces induce too much agglomeration. Martin (2000) identifies three potential market failures. First, localised technological spillovers may result in too little agglomeration, if the agglomeration externalities are under-rewarded by those who realise these activities. Hence, it is indeed possible that there is too little agglomeration from the point of view of overall growth. Second, neglect of the welfare of immobile individuals in poor regions may cause too much agglomeration to occur. The reason is that the remaining inhabitants in the peripheral areas are hurt by negative externalities from out-migration in terms of a smaller labour market, making job matching more difficult. In addition, consumption becomes less divers and more expensive and, if mainly individuals with high human capital move, the amount of spillovers that occurred from them to other workers will disappear. In this case, the problem is rather a lack of concentration in rural areas, and a partial solution is to increase the mobility of individuals. It is also an issue of redistribution, and the question is whether regional policy necessarily is the most efficient measure to address equity matters. Third, distance can aggravate

imperfect competition, by exaggerating the market power of firms close to consumers in peripheral areas.

Social capital

Over the past decades, economists have increasingly been interested in the connections between social capital and economic performance. Especially, the role of social capital in rural development has been emphasised. Most of the studies focus on developing countries, but some applications to the CEECs have been carried out as well. There are several definitions of social capital, the main elements being aspects like associations, organisations and networks, and cognitive elements such as shared values, norms, attitudes and trust.

Social capital is argued to play an important role in shaping economic outcomes, as it can lower transaction costs, strengthen informal insurance mechanisms, increase probability of trust-sensitive exchanges, enforce contracts and facilitate credit at the level of individual investors, in addition to, improving local authority performance by drawing them into networks. In rural regions, social capital can help people to perform several tasks more efficiently: mobilise resources and manage them, communicate with other, and co-ordinate activities and help to solve conflicts.

Knack (1999) summarises several studies on social capital: "… most of the evidence provides strong support for the hypothesis that social capital, as measured at national level, is associated with improved economic welfare of societies as measured by growth, investments and poverty indicators". According to van Kooten *et al*. (2001), institutions and social capital, especially effectiveness of government and trust, are important variables explaining why some countries in Eastern Europe exhibit better economic performance than other. Suchanek *et al.* (2002) shows that trust itself is a function of the institutional environment and they conclude that the government has an important role to play in creating the proper institutional surroundings for economic success.

Assessment of existing rural development policies in the EU

Components of rural development policies in the EU at present

The present framework for rural policy within the European Union consists of three sets of regulations. Those include the Regulation for Rural Development (RRD, Reg 1260/99), Structural Funds (SF) either in objective 1 (regions lagging behind), or objective 2 (conversion of areas facing structural difficulties), and the LEADER+ Community Initiative.

The RRD is the so-called second pillar of the CAP. In contrast to the first pillar, which is based on annual payments, and focuses on individual commodities and applied uniformly across the Union, payments within the second pillar are multi-annual, programming based, menu driven, and regionalised. The measures included in the RRD can be divided into two categories; sectorial and territorial. The former are directed only towards agriculture and are the same for all rural areas, while the latter are applicable outside agriculture and may be different in each area, and can therefore be adapted to specific rural conditions. The sectorial measures are well articulated and cover a wide range of farming needs, like facilitation of structural adjustment, permanent assistance to perceived handicaps in particular areas and provisions for environmentally friendly agriculture, while the territorial measures are more recent and, in contrast, appear less articulated (Saraceno, 2002). Their major rationale is the diversification of activities in rural areas. Consistency with other instruments of the CAP requires some basic support criteria at Community level, in order to ensure compatibility and to avoid distortions. As a result, the "menu" of measures seems rather detailed, but different MS are free to compose their own "a la carte".

The Structural Funds, the EU's regional development policy, was established already in the 1970s. The EU specifies criteria for eligible regions and areas, while the content of the "programming documents", in accordance with some priority objectives, primarily is the responsibility of the member states. The SF can finance interventions in objective 1 and 2 areas with respect to infrastructure, tourism, small and medium enterprises, and the environment through specific programmes. This means that territorial functions are included in the interventions of the SF instead of in the rural development programmes. In addition to some major investment projects, the SF money provides support for market studies, pilot projects and exchanges of experience in order to promote innovative practices through simple and transparent implementation. Overall, the SFs' early actions failed to reduce regional economic disparities due to the lack of resources, lack of continuity of regional actions, and absence of clearly defined priorities. Still, although reformed, the EU's regional policies have been found to mainly serve a redistributional purpose instead of promoting growth in laggard regions (Boldrin and Canova, 2001).

The third form of EU intervention in rural areas is the LEADER+ initiative. It is a locally based bottom-up approach, implying participation of local actors and a formal establishment of partnerships, between private and public local interest groups. It is intended to be an integrated approach, including linkages of all relevant sectors of the local economy in a coherent strategy for the future, and is intended to promote networking activities between different local groups. The main instrument is time limited project support and the intention is to initiate a sustainable development process.

In Table 1, columns 1-3 provide a description of the different measures provided, and column 4 includes a justification of the measure in terms of the perceived market failures or equity objectives. It should be noted that those validations are not any official justification. The intention is rather to ask what kind of economic malfunctions that could justify the measure in question. Concerning the coverage of policy measures, it can be noted that the Table does not include every single measure currently in place, since member countries, to some degree, can design their own policy measures and a variety of specialised measures exist. Instead, Table 1 covers the main policy measures in order to give a comprehensive picture of the general state of affairs regarding support measures.

Targeted market imperfections

Several types of economic policy instruments are used. A capital grant is a subsidy that finances part of an investment and the receiver of the grant, most often a farmer, is obliged to pay a part of the investment from his/her own means. Several of the measures are directed to the starting-up of some kind of services or activities, *e.g.* farm management service, although not supporting the operation of the activity once it has begun. It is also possible to receive support to conduct market research, etc. Support to programming services within the Leader+ Initiative is intended to pay some of the costs incurred by pilot strategies aimed at developing the potential of rural areas, and is not intended to support productive investment nor investment in physical infrastructure.

Table 1. Measures of the Regulation for Rural Development (RRD), of the Structural Funds ERDF and ESF and of the EAGGF Guidance Section, LEADER+

Category	Measure	Economic instrument	Justification
RRD - aiming at farmers			
Investments in farms	Investment in agricultural holdings	Capital grant	Capital market imperfections, income support
	Land improvement	Capital grant	Capital market imperfections
	Reparcelling	Capital grant	High transaction costs
	Restoring potential after natural disasters	Capital grant	Missing contingency markets
	Setting up of young farmers	Capital grant, interest rate subsidy	Income support, transaction costs
Processing and marketing, aiming at farmers' income	Processing and marketing of agricultural products	Capital grant for investments	Income support
	Marketing of quality agricultural products	Support to marketing	Diseconomies of scale, transaction costs
Service and infrastructure for farmers	Farm relief and farm management services	Support to set up services	Insufficient technology diffusion, income support
	Agricultural water resources management	Education	Insufficient technology diffusion, public goods
	Infrastructure for agriculture	Support to set up activities	Insufficient technology diffusion
	Financial engineering	Information	Capital market imperfections
Human resources in farming	Early retirement	Early retirement pension	Income support, facilitate structural adjustment
	Training	Education subsidy	Capital market failure, deficiencies in education system, information failure
Less favoured or environmentally sensitive areas	Compensation to farmers	Payment per hectare	Income support, external effects, public goods
Forestry	Afforestation of agricultural surface	Payment per hectare	Income support
Environment	Agri-environmental schemes	Payment per hectare	Public goods, external effects
	Other forest measures	Capital grants (partly), information	Public goods, external effects
RRD, SF and LEADER+ - aiming at rural inhabitants			
RRD Promoting the adaptation and development of rural areas	Basic services: rural economy/ population	Support to set up services	Equity
	Rural heritage and village development	Capital grant	Public goods
	Diversification of agricultural activities	Support for market research and pilot projects	Income support, equity, transaction cost
	Promotion of tourist and craft activities	Support for market research and pilot projects	Transaction costs
SF Objective 1 and 2 measures to specific rural areas	Programming documents	Support for market research and pilot projects	Transaction costs
	Major projects	Capital grants	Insufficient physical infrastructure
	Innovative programme	Capital grants (partly)	Transaction costs
LEADER+ Rural areas, with ageing population, and rural depopulation which persists in some areas, and job losses	Integrated territorial rural development strategies	Support to programming activities	Transaction costs, capital market failure
	Interterritorial and trans-national co-operation	Support to programming activities	Transaction costs
	Networking (mandatory)	Support to programming activities	Social capital defiance

As can be seen in Table 1, several of the measures in the RRD are aimed at promoting investment, and the basic hypothesis in a neo-classical growth framework would be that such measures could foster growth by increasing the rate of capital growth. Hence, if capital market failures mitigate investment in rural areas, the rate of capital growth, and hence output growth, will be too low. However, although there could be an undersupply of credit in rural areas due to information failures, it can be difficult for government officials to distinguish good projects from bad ones, resulting in an over-supply of credit to projects that are bound to default, which is an expensive and inefficient use of resources. A capital market failure, as such, does not motivate a subsidy element in the credit, like an interest rate lower than the market rate, or that the government finance part of the investment, as such a subsidy primarily has a redistributive purpose. Addressing equity issues in this way introduces an unnecessary distortion by making agricultural investment seem more profitable than other investments, a distortion that counteracts the diversification of the rural economy. It should also be noted that labour tends to be replaced by machinery as a consequence of the investment subsidy, since machinery is becoming relatively cheaper compared to labour, because of the subsidy. This measure hence contradicts the overall objective to promote employment in rural areas.

Objectives concerning the environment and multifunctionality motivate some of the measures. In order to mitigate negative externalities like environmental decay and promote the provision of desirable positive externalities, some of which having the character of public goods like for example biodiversity, specific and directed measures are essentially a good idea. Both the presence of externalities and public goods are classical examples of market failures that can be effectively addressed by directed measures. The phrase “directed measures” should, however, be emphasised since a potential problem is that some of these objectives, especially the provision of positive externalities from agriculture, are addressed in an indirect way. In addition to being unnecessarily expensive and inefficient this approach could in fact counteract the whole intention of the measure.

Some of the measures are motivated by high transaction costs. Depending upon the level of development, transaction costs can be high, because of deficiencies in the overall economic and institutional framework. In that case, resources can generally be more effectively used if directed to promote the overall business climate, enhance the socio-political framework and counteract the often prevailing negative bias against small enterprises, which is harmful for small firms in general, but particularly cumbersome for small firms located in rural regions. However, specific measures intended to reduce transaction costs that are part of a structural adjustment process, like the costs of reparcelling, can be sound in order to facilitate an ongoing process. In addition, transaction costs are generally higher in rural areas because of the distance to economic centres and lack of agglomeration effects. The magnitude of this problem can diminish with a high level of social capital in the area.

It is more difficult to attempt a classification of measures included in ESF/ERDF and LEADER+. The measures are mainly directed to short term projects. The underlying assumption is that a lot of good ideas are present in rural areas, and that these ideas have a potential to be commercialised into viable business projects generating incomes and employment but, due to certain deficiencies of rural areas, this commercialisation fails to take place. If there are high transaction costs in terms of finding out whether a particular idea has a market value, or there is a high risk associated with starting up a business activity or diversifying an existing firm, it is possible that viable projects never take off. Project support aimed at, for example, financing market research in order to investigate whether a particular business idea is worth pursuing, can hence be motivated on efficiency grounds. There is, however, a risk that recipients come to rely on project support as a form of income support, by jumping from project to project, so that the support basically becomes a transfer of income. This is particularly the case if there is a genuine lack of business opportunities in the area, that is, if the inhabitants, in fact, do not have good unexploited ideas. In this case, it is very difficult to create such opportunities with a mere income transfer. In addition, negative effects in terms of ‘project fatigue’

may arise, if individuals engaged in projects that fail to generate any lasting effects lose their entrepreneurial spirit (Havnevik *et al.*, 2001). On the other hand, it is also possible that the project process itself helps to build social capital, meaning that although the direct outcome of a particular project is meagre, the resulting enlarged social capital may facilitate future business ventures. However, in societies where people trust each other and government institutions, the marginal benefits of further investments in additional social capital is limited. Project support can also be motivated by capital market failures, but it is unlikely in a well-developed economy that capital market failures are so severe, that it is impossible for a well established rural inhabitant to borrow money for a sensible business project. Hence, to some extent, this type of support can serve a purpose by reducing high transaction costs and risks, when unrealised business opportunities do, in fact, exist. However, substantial spending on these types of projects can hardly be justified.

The direct, and sometimes indirect, objective of several measures is to support farm incomes. This is purely a redistributional motive, constituting of a transfer of income from taxpayers and consumers to farmers. Equity considerations are a justifiable reason for state intervention, although this type of intervention differs to a significant extent from the correction of market failures previously discussed, since the intention is not to make the economy function better, but to spread the overall gains from economic activities more evenly among the inhabitants. This purpose can be achieved in several ways and the principal rule is to choose the less distorting, most efficient measure, in order to avoid unnecessary costs. The effectiveness of the above measures can be questioned in several respects, for example, since they are not targeted to farmers most in need. Overall, they are generally inefficient and expensive in supporting farm income (OECD, 2002).

Finally, it should be recognised that the process of pursuing ambitious rural policies is costly as such, and that the resources absorbed have alternative uses. In particular, current EU programming, approval and accounting procedures bind significant administrative resources, in particular, in less developed regions, that might be more effectively used elsewhere (Baldlock *et al.*, 2001). The substantial delay in finalising the SAPARD plans in practically all the CEECs illustrates the difficulties involved very well. Furthermore, rural development measures often have a rather narrow focus on agriculture, but it is important to address not only farmers but all entrepreneurs in rural areas. Otherwise, it is possible that direct support to the agricultural sector has an indirect negative impact on non-agricultural entrepreneurs, counteracting a needed diversification of the rural economy.

The role of rural policies vis-à-vis general policies

A conclusion that emerges from the discussion above, is that, with the exception of the environmental payments/programmes, which indeed addresses market failures,[3] rural development policies in the EU cannot be characterised as an efficient response to market failures that are likely to prevail in rural regions. The policies concentrate on income redistribution rather than on the correction of market failures and focus too strongly on agriculture and on project support and tend, moreover, to address general problems with specific measures. This raises the issue of the place of rural policies in relation to other societal policies or, simply, the question which rural problems should be solved by directed policies. This question is particularly pertinent with respect to redistributional measures.

In many countries, it can be observed that the relative size of the transfers to rural areas induced by general policies often dwarf funds provided through pure regional policies. For instance, both tax policy and social policy have major implications for the well being of rural regions. To put it simply, if

3. Whether the environmental support in place in various MS actually guarantee an efficient delivery of public goods and correct negative externalities or constitute, as sometimes claimed, in effect an income support in disguise is another issue, which falls outside the scope of this paper.

these policies contribute to an equalisation of disposable incomes among individuals, a reasonable equalisation between the regions will follow as well. In addition, these transfers are generally more efficient when it comes to levelling out income disparities between individuals. Hence, specific rural policies that only deal with income transfers must have an additional value to justify their implementation. Further, not all individuals in a poor region are in fact poor, just as not all individuals in a rich region are rich. By focusing on regions rather than individuals, there is a potential risk that income transfers between regions through directed rural policies could come at the expense of poor individuals in rich regions.

With respect to measures that aim at improving efficiency, rural policies should focus on market failures that are specific to rural regions or strongly exacerbated by rurality. However, it should be also noted that policy implications that emerge from the agglomeration and the new trade and growth theories are not clear-cut, and may involve a trade-off between the overall national growth rate and regional inequalities. Some policies, such as measures that improve the quality of human capital in rural regions or lower the cost of transport may enhance the welfare of individuals who move away, but harm local development.

Another important issue is whether existing general polices are spatially neutral or entail a hidden urban bias, a bias that directly or indirectly put rural areas at an artificial disadvantage. There may also be a hidden bias to the disadvantage of small firms and, consequently, to rural regions, since the economy of such regions is dominated by small-scale activities. In Canada and the UK, for example, policy makers actively try to reduce the pro-urban bias in economic and social policies, by correcting the result of other polices applied at the country level.

Rural regions and agriculture in the Baltic countries

The theme of this seminar is rural policies for the Baltic countries. Before starting the discussion on issues that are specific to the Baltic region, some basic facts are necessary. About one-third of the population lives in rural regions in the Baltic countries. The situation in rural regions differs, however, quite a lot between the countries. In Lithuania, almost one-fifth of the population is employed in agriculture, and the average size of a farm is 7 hectares. In Latvia, the share of agriculture in employment is 13.5%, and farms are larger on average, 18 hectares. Estonia is not too dissimilar from some of the present members, with 7.4% employment share and an average farm size of 20 hectares. Estonia, in turn, has experienced a dramatic decline in agricultural labour. In Lithuania, labour use in agriculture increased while Latvia has experienced a moderate decline. A decline in agricultural terms of trade, caused by price and trade liberalisation and a cut in consumer and producer subsidies, reduced profitability and hence demand for labour in all CEECs. To some extent, this was offset by the substitution of other inputs by labour, which increased the demand for labour (Swinnen *et al.* 2001).

The process of transition to a market economy has been successful, but many difficulties remain in rural regions. Analyses conducted in the Baltic countries in the process of preparation of SAPARD programmes reveal several problems and challenges. These can be divided into two categories:

- **Problems related to agriculture:** Land is fragmented due to the restitution of historical boundaries and farms are very small in Lithuania. The access to credit is low, machinery is outdated, market access is poor, there is weak development of co-operative activities, and land markets do not function properly. Further, the food processing industry is inefficient due to overcapacity and lack of machinery.

- **Problems related to rural areas:** Overall, the rural physical, economic and social infrastructure is underdeveloped. Examples are the absence of representative organisations and networks, and the poor quality of roads, electricity and housing. Incomes in rural areas are generally low, especially in agriculture, and are often related to a decline in agriculture. In addition, the overall level of education is low, meaning that there is a lack of skilled labour and also, that the experience needed to start up businesses is insufficient. The age-structure is generally unfavourable, a situation which is aggravated by out-migration of young people. Finally, structural unemployment is persistent and alternative employment opportunities are in short supply.

A key issue for policy design is to identify market failures that are specific to transition countries, or exacerbated by the process of transition, as well as other factors that are inhibiting growth and development in rural areas in the Baltic countries. Concerning market failures, capital market failures are prominent since the land market is still not functioning properly. This may have an impact on investment activities, since land is used as collateral, as well as structural change in the agricultural sector. Lack of competition is a problem, with monopoly/monopsony power in input supply and processing. Transaction costs are high due to deficiencies in social capital (van Kooten *et al.* 2001) and institutional weaknesses, and the lack of contingency markets is a problem. However, the emergence of institutions of vertical co-ordination has facilitated enterprise development by bridging some of the market imperfections. Contracting with upstream processors has had a significant impact on technical efficiency and membership in a co-operative generally increases the efficiency of commercialisation (Swinnen *et al.* 2000).

Factors inhibiting establishment and growth of enterprises, both within and outside agriculture, in addition to market failure are imperfect property rights, low human capital, and credit and finance constraints (Swinnen and Gow, 1999). In addition, the generally low level of income constrains the possibilities to develop private local services.

Policy implications for the Baltic countries

In several aspects the situation in the Baltic region is very much different from the situation in the present EU members. In the West, agriculture and rural has ceased to be synonymous, and non-agricultural employment dominates in rural areas. The standard of living is generally high, especially in the middle-class commuter belts, and among farmers, pluriactivity is prevalent. However, the present conditions are not a result of past policies, rather the development has occurred in spite of them (Saraceno, 2002). In particular, the CAP has not prevented agricultural employment from falling. In contrast, agricultural employment is still significant for rural employment in the Baltic countries, especially in Lithuania.

What can be concluded from the previous discussion of the Baltic countries? To start with, it should be observed that rural areas, just like urban areas, have several general problems. For instance, an important pre-condition, which is also valid for the economy in general, is the existence of an institutional structure that is conducive for small firms and of entrepreneurial activities through stable rules of the game. What is needed are, *inter alia*, legal systems which secure property rights, together with taxation and credit policies which create incentives and equal opportunities for small enterprises, in particular, for rural entrepreneurs. Issues like this should be addressed by general policies, not specific rural policies. Furthermore, general social and economic policies are of key importance. Obviously, one should have only modest expectations on what can be achieved by specially designed regional/rural policies. A range of non-rural policies need to work properly for rural policies to be sustainable. There is considerable poverty in rural regions, but social/tax policies are generally more efficient when it comes to redistributing income. The history of the CAP shows, in particular, that

pursuing social concerns through sectoral policy does not work, and it is doubtful whether rural social policy will work either.

Massive and fast out-migration of the rural population is socially disruptive and economically costly. Thus, there are good reasons for slowing the process down to some extent. It is, however, very difficult to find justifications for policies aimed at preserving the present pattern of settlements. Especially in the early stages of economic development, an increased concentration of the population and economic activity may be difficult to avoid, even at very high costs. Agriculture is an important sector in rural regions of the Baltic countries. Hence, the development of agriculture is important for the development of rural areas. However, an agro-centric view of rural development, which still prevails in the EU, would be harmful for the future prosperity of those regions in the Baltic countries. The CAP could not prevent agricultural employment from falling in the west, and a diversion of resources to agriculture in the east is not likely to contribute to sustained rural employment either. Growth of labour productivity will unavoidably imply that fewer people are engaged in the production of food. Agriculture and forestry are both capital intensive and diminishing sectors, meaning that government induced job creation in those sectors will be very costly, as indicated by Swedish experiences (Ds 1989). Thus, policies aimed at developing agriculture should be co-ordinated with rural development policies into an integrated rural development approach.

General principles for rural development policies, as identified previously in the paper, apply equally well to the Baltic region. Such a policy should focus on the removal of prevailing market failures, provide substitutes for some of the benefits of agglomeration, actively remove the urban bias in government policy, and focus on social capital building. In addition, it is important to enhance the national social, economic and physical infrastructure. This is especially important in the rural regions of CEECs, where a system of modern rural institutions, like an efficient banking system, regional job centres, notary offices and, legal and economy advisory services, by and large, are lacking (Duzckowska-Malysz, 1996). The policy should also include technical assistance to rural development projects, consisting of feasibility studies, advisory services and professional management, as well as investment assistance for new enterprises. Developing local marketing systems and networks of producers is also advisable. Considerable economies of scale can exist in the co-ordination of activities such as marketing and delivery of products and services of small rural firms, in particular, such as rural tourism, regional specialities, off-farm activities based on farm labour and farm machinery. Rural development policy may help to facilitate the process of taking advantage of such economies of scale by fostering co-operation among producers, in particular, in countries that lack co-operative traditions in the countryside. However, it should be observed that policies of this kind are motivated to the extent they bridge prevailing market failures and aim at promoting a self-sustained growth through seeding of local enterprise. When genuine market prospects are missing, support to market research or feasibility studies will not produce any lasting benefits.

Another fundamental issue relates to the development of human capital. In order to encourage social mobility, which is a precondition for long term equalisation of incomes and social conditions between rural and urban regions, a range of education and vocational training, not confined solely to farming, needs to be provided, especially retraining and provision of non-farm skills and knowledge. Development of rural areas also requires that these areas are competitive from the point of view of quality of life. The reversal of the rural-urban migration trends, which can be observed in many rural regions in the OECD countries, was, as pointed above, triggered by the high quality of life in rural areas. Thus, improving the quality of rural life by the provision of infrastructure and services like transport services and childcare, would greatly enhance the competitiveness of rural areas and counteract out-migration of young and entrepreneurial people.

It may be presumptuous, especially in a short paper, to pass judgement on the tremendous efforts spent on the preparation of the Baltic SAPARD programmes. However, the structure of the spendings seems to replicate the similar bias that can be observed among older members of the EU. The focus on agriculture and food processing seems too strong and the policy seems not to be much concerned with market failures. The challenge of adjustment to the *acquis* may justify spending money in the short run, on improving standards in food processing, but in the long run diversification and development of activities outside traditional agriculture can better solve the problems of agriculture and rural regions. In terms of spending, the focus on environmental measures in Baltic SAPARD has been insignificant. Spending money on environment may seem an unnecessary luxury when so many pressing challenges are present. However, the process of agricultural development in the West has involved a lot of irreversible degradation. It would be a pity if the same developments were replicated in the Baltic region. Moreover, an attractive natural environment contributes significantly to the attractiveness of rural regions as places to live in or sites for leisure and tourism.

Concluding comments

This paper has examined whether measures that are available in the framework of rural policies in the EU constitute an efficient response to market failures that are likely to prevail in rural regions. The main conclusion is that this seems not to be the case. Policy measures appear to concentrate on income redistribution rather than on the correction of market failures, and focus too strongly on agriculture and on project support.

Integrated rural development programmes cannot be perceived as a panacea for all rural problems. In particular, a choice must be made about a proper division of tasks between general policies and specially designed rural programmes. With respect to measures that aim at improving efficiency, rural policies should focus on market failures that are specific to rural regions or strongly exacerbated by rurality. When it comes to income redistribution, it could be observed that tax and social policies constitute a more efficient way of transferring income than pure rural policies. Especially, it should be recognised that the main solutions to the rural problem must be found in general economic growth and development, as well as in a general improvement of the functioning of the economy. Extensive subsidisation of agriculture is not a solution to rural problems, as the experience of western countries indicate. Neither is, however, an extensive subsidisation of rural regions in general. A major effort has to be devoted to the removal of barriers and obstacles and to foster a self-sustaining process of rural growth. Creating enabling institutions and infrastructure development are key elements of a successful development strategy.

An explanation for the poor record of regional and rural policies in stimulating growth in laggard regions in current EU members so far, could be that the existing policies have tended to focus on non-existing market failures, or in effect, addressing equity issues when trying to enhance the efficiency of the economy. Equity is a perfectly legitimate reason for public intervention, resting on a politically formulated vision regarding what is fair, but obtaining equity goals by income transfers does not generate growth or development *per se*, since the basic malfunctions of the economy have not been addressed. There are, though, certain measures that could be conducive to both growth and equity, for instance, the provision of basic services to rural areas, since the provision of childcare, medical service, etc., have a positive effect on the degree of access, as well as supports local development by providing the underlying structure needed for the local economy to function.

In addition to the prevailing mix-up of equity and efficiency regarding the choice of policy measures, and the notion that separate measures are generally needed to address different, perhaps conflicting, goals, it is common to regard conservation and development as synonymous concepts. It is, for example, common to say development, but mean conservation, when talking about the

countryside. However, development is an ongoing evolutionary process, which not necessarily preserves old settlement patterns or existing means of survival, but creates new opportunities and new imprints in the rural landscape. For instance, a modern and efficient agricultural sector may not provide society with all the positive externalities that traditional agriculture used to do. The solution is not to try to prevent agricultural modernisation, but to seek other means in order to preserve attractive features of the cultural landscape. This is not to say that conservation and development are always conflicting goals, but rather that development may, or may not, preserve, the current feature of rural areas. Hence, it is important to be precise when defining the objectives and also to be clear about cause and effect when constructing policy measures.

A further unclear matter in the debate concerns the distinction between regions as opposed to the distinction between individuals. Is it actually inequality between individuals or between regions that matters? If the underlying objective is to achieve higher equality among individuals, measures seeking to enhance regional equality may not be optimal. A similar issue is raised by Puga (2002) who asks, with respect to the Structural Funds, whether the objective should be homogeneous across space of certain aggregate measures, such as income per capita, unemployment, health or education, or homogeneous of personal fairness, that is similar people having similar opportunities in different places. For example, should rural policies encourage mobility, which can enhance incomes and welfare of those moving, even if this is a threat to some rural areas that are being drained of young educated people, or should they aim at combating out-migration and preserve today's settlement patterns.

Finally, it must be realised that what policy makers want to do, does not always correspond to what policy makers can do. The government cannot create substantial employment in rural areas - only provide a good environment for jobs to be created. It is not possible, or even advisable, to try to reverse a general trend of urbanisation, especially not in countries undergoing a transformation process in which modernisation of the agricultural sector is taking place - like the Baltic States. Since 10-20% of the work force is currently working in agriculture only a labour intensive industry could absorb all the labour released from agriculture. Hence, pluractivity among farmers is not enough to support employment in rural areas in these countries. Instead, enhanced labour mobility between sectors and regions, in combination with education and vocational training are important elements in supporting the development process.

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STRATEGIES FOR LOCAL DEVELOPMENT IN RURAL AREAS

By Professor P. Joseph Mannion, Ms. Monica Gorman and Dr. James Kinsella
(Paper presented by Prof. J. Mannion)

Abstract

Against a background of declining population in many rural areas of Europe, declining farm incomes, too few other jobs and in some areas, inadequate services, there is need for a comprehensive policy for rural development and for re-orientation in skills and activities to exploit rural indigenous resources. This is the fundamental challenge which the European Commission started to address in the 1992 agricultural policy reforms, continued through the implementation of the Agenda 2000 Agreement in 2001 and is now being re-negotiated in the 'Mid-term Review' of Agenda 2000. It is appropriate to underline the significance of these developments for the Baltic countries.

Against the stated purpose of this part of the Seminar ("…to identify suitable rural and regional development approaches..."), it is appropriate to note Commissioner Fischler's vision for an EU rural development policy: "The aim is a Community Policy which takes into account all aspects of Rural life – the economic, social and cultural. Which is why it goes well beyond agricultural policy (Fischler, 1996, p. 2)." The aim of local development strategies in rural areas is to have ***'A Living Countryside'****. Part one of the paper sets out what is involved in achieving this outcome. In Part two, the main elements and the lessons learned from the operation of LEADER (the EU Community Initiative) in Ireland are presented. Part three focuses on the potential of the LEADER area based development approach for the Baltic countries.*

Part 1. A living countryside

A living countryside and multi-functional agriculture

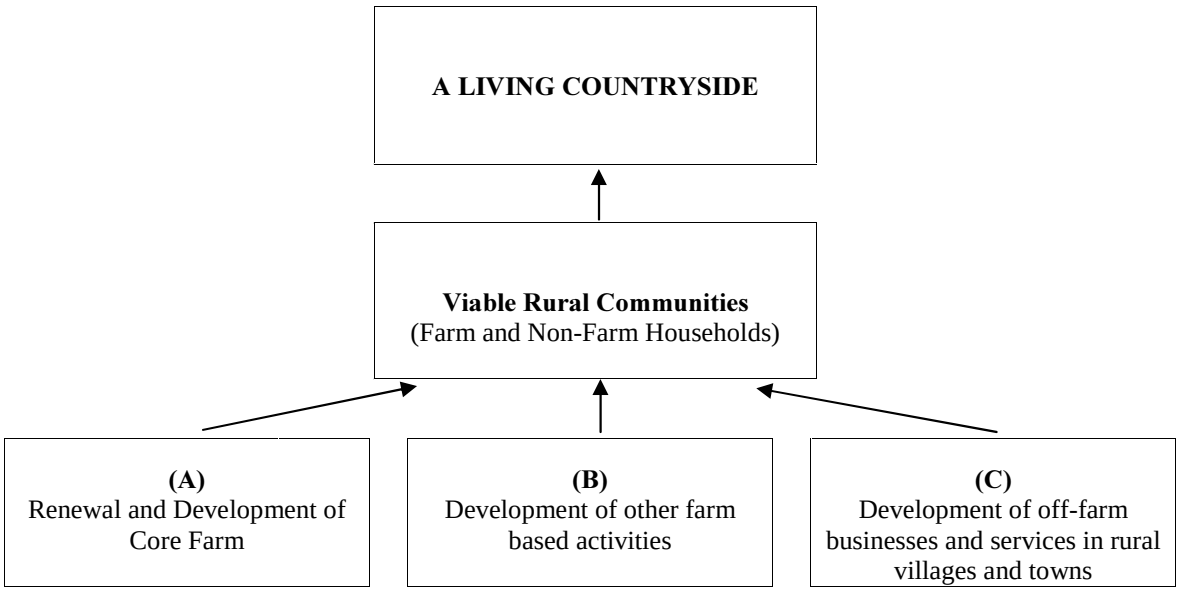
The rural context is continuously changing. Farmers in Europe constitute an ever smaller section of the population and the consumer's point of view carries increasing importance. Agriculture and rural policies are increasingly targeted to serve society as a whole and there is increasing demand by European society for public goods provided by agriculture – environment and animal welfare, high quality landscapes, etc.

The production of food and fibre remains a primary function of agriculture, but there are growing concerns about the dangers of intensive production. It is generally believed that more extensive farming systems contribute to the quality of the landscape and bio-diversity.

The notion of a living European countryside implies a unity between agriculture, society and the environment. The Cork Declaration articulated the commitment of the European Commission to multi-functionality stressing that agriculture is, and must remain, a major interface between people and the environment, and that farmers have a duty as stewards of many of the natural resources of the countryside. Van Depoele (2000) emphasised the value which European society places on the contribution of agriculture to the viability of rural areas and a balanced territorial development. Many remote and peripheral areas offer few other possibilities of gainful employment.

To create the reality of a living countryside, people must be able to make a qualitatively good living from the countryside *i.e.* to construct sustainable rural livelihoods. European agricultural and rural development policies attempt to foster this 'living countryside' through a variety of mechanisms. The model shown (Figure 1) of a living countryside places farming in a vital role, producing food and fibre but also being broadened and diversified to provide other goods and services and complemented by a range of off-farm enterprises and services which enrich the quality of life in rural areas (Kinsella, *et al*., 2000).

Figure 1. The Key Components of the Living Countryside



This model suggests the need for conventional agriculture (A) to be revitalised so that production of food and fibre is competitive and maintains its position in the broader economy. The second area (B) is the development of other farm based activities, the broadening of the products of agriculture to create goods and services that are valued and can yield an economic return, highlighting the need to reinforce the multi-functional nature of farming. The third area (C) is the wider rural economy, which enables the businesses and services to create a vibrant rural society and economy.

The challenge in creating the 'living countryside' is reconfiguring the role of agriculture and the individual farm household in rural areas.

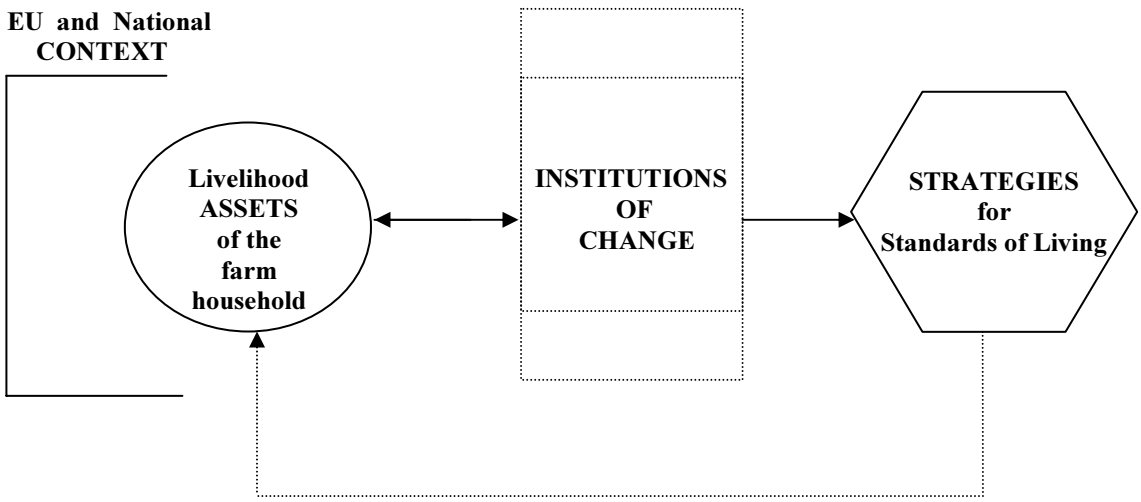
Farm household livelihood strategies

Farm families employ a variety of strategies to ensure their livelihood. These strategies enable them to convert their assets or resources into goods and services that are valued by society and that can earn them a satisfactory income. Figure 2 is useful in understanding the factors that influence the livelihood strategies of farmers.

The changing context influences the base of livelihood assets people can draw on in securing acceptable living standards. The changing demands of European society, obligations from global agreements, and European and national policies all influence the context within which farm families construct their livelihood strategy to maximise newly created opportunities and to buffer themselves against constraints.

The livelihood assets of farm households are the human; economic; environmental; social; cultural and political resources available to them from which to draw their livelihood and ultimately achieve an acceptable standard of living. Human assets include skills; knowledge; self-confidence and motivation. Economic assets include land, capital and labour. Environmental assets include landscape features; habitats; clean air and water. Cultural assets might include the history; folklore; cultural heritage; gastronomic traditions and language of a particular locality. Social and political assets could include the extent to which people belong to networks that enhance their quality of life or enable them to have influence over decisions and policies that affect them. The value and importance of the different assets evolve and change with contextual changes. What once was an important asset giving access to certain livelihood strategies might lose its value due to changes in the political or economic context or changes in the context might open up new opportunities for alternative strategies. Land that was once considered to be of low value because of its limited potential for agricultural production might now be considered an asset because of its environmental qualities.

Figure 2. Livelihood Strategies of Farm Households



The relationships between the context, the assets and the actual livelihood strategies which people adopt are influenced and mediated by institutions including governments, policies, regulations, support agencies and services, etc. These institutions can enable or inhibit the development of certain livelihood assets and strategies. At the same time they influence the context within which livelihood strategies are constructed.

Rural development – expanding the pool of livelihood assets

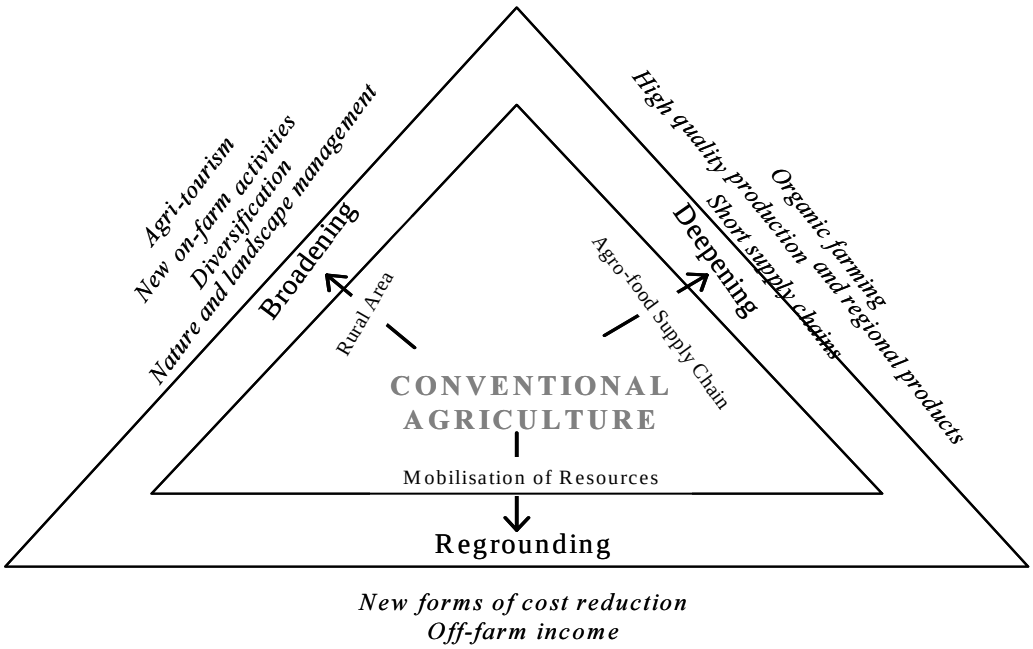
Using the model of rural sustainable livelihoods, rural development can be seen as an attempt to increase the 'pool' of livelihood assets with which farm families construct their livelihood. Specifically the rural development paradigm seeks to revitalise the interaction of agriculture's three dimensions by *broadening*, *deepening* and *re-grounding* the role of conventional agriculture – as illustrated in Figure 3 (van der Ploeg *et al.,* 2002).

Broadening refers to the development of on-farm non-food activities which create new sources of income and employment and are oriented at newly emerging markets *e.g*. nature and landscape management, agro-tourism and new on-farm activities.

Deepening refers to those activities which extend the involvement of the farm in the food supply chain beyond primary production of commodities by taking charge of food processing and marketing or guaranteeing specific product qualities *e.g.* in organic farming, direct selling and high quality food production.

Re-grounding refers to a different alignment of human and natural resources towards more sustainable forms of agriculture and includes off-farm employment and new forms of cost reduction such as decreasing external inputs.

Figure 3. The Structure of Rural Development at Farm Enterprise Level



Findings from a three year study (van der Ploeg *et al.*, 2002), which examined the socio-economic impact of rural development in the EU-15, indicate that deepening, broadening and re-grounding activities now account for almost half of the EU farm household income. Corresponding data for Ireland (Gorman, *et al.,* 2002) are shown in Table 1.

Table 1. Estimated Overall Impact of Rural Development in Ireland

ACTIVITIES	As a % of National Farm Household Income
Deepening (Organic farming; quality production; on-farm processing; direct marketing)	**0.5%**
Broadening (Agri-tourism; REPS new economic activities; Non-food production; energy production)	**4.7%**
Re-grounding (Off farm employment, cost reduction)	**44.9%**
Rural Development **Total:**	**50.1%**

Implications for local, rural area, development

Using these conceptual frameworks (the living countryside; sustainable livelihood strategies and a rural development paradigm of broadening conventional agriculture) we can get a better understanding of possible regional farm and non-farm development options and strategies. The frameworks are helpful in identifying and assessing the policy instruments and mechanisms required to achieve the desired outcome – A Living Countryside.

In designing strategies from local development in the 'Baltic 3' (Estonia, Latvia and Lithuania) for the coming years, there are significant messages and challenges in what is evolving in the EU 15 in relation to agriculture and the development of rural areas. In this regard, strengthening civil society – its local institutions and the participation of people in development decisions – should be seen as a crucial step. The LEADER Community Initiative has played a vital role in participative redistribution and rural area development, particularly in countries such as Ireland, Spain, Greece and Portugal. The LEADER experience in Ireland and possible lessons for the Baltic 3 are presented in parts two and three of the paper.

Part 2. The LEADER programme in Ireland

The LEADER programme in Ireland was launched in 1992 and has, since its establishment, secured a high profile at local, regional and national levels in the development of rural areas. LEADER in Ireland is synonymous with rural development. The LEADER programme has, since its establishment in 1992 to 2002, been administered at national level through the Ministry of Agriculture which is the 'intermediary body' between the Commission and the LAGs. In autumn 2002, responsibility for the operation of LEADER was assigned to the Ministry of Community, Rural and Gaeltacht Affairs.

LEADER I (1991–1994)

In Ireland there were 17 local action groups (LAG) involved in the LEADER I Programme and they covered approximately 60% of the land area of the country. The areas represented had an average population of 62 500 people and covered, on average, 2 500 km^2. The LAGs were managed through 'boards', which were formal partnership structures, and which were responsible for the implementation of the local area programmes. The LEADER boards averaged 14 members and were made up of representatives of community groups (average of 36% of members); the private sector (29%); state agencies (21%) and local authorities (14%). The majority (65%) of the groups had been in existence before the LEADER programme, while the others were established to avail of LEADER support (Kearney *et al*., 1994).

The total public expenditure (EC and Irish government) in LEADER I was EUR 44.5 m. The measures which received the LEADER I funds in Ireland were: rural tourism (51%); small enterprise such as crafts, engineering and furniture-making (20%); and natural resources including agricultural and horticultural production, as well as food processing (19%). Vocational training and other technical support received 8% of the LEADER I funds.

LEADER II (1995-1999)

LEADER II began operations in Ireland in 1995 and increased the number of LAGs to 34 and three other collective actors and covered almost all rural areas of the country. Of the 34 LAGs approved for LEADER II, four were categorised as 'pre-development groups' and were allocated funding to assist in their progression towards full involvement in the programme over the following year (1995/6). The 34 rural areas represented had an average population of 67 500 people and covered, on average, 2 000 km^2. The LEADER II boards had typically between 16 and 17 members and were made up of representatives of community groups (average of 40% of members); the private sector (30%); state agencies and local authorities (30%).

The total public expenditure (EC and Irish government) in Leader II was EUR 119.5 m, while this was invested in: animation and training (27%); rural tourism (23%); small enterprise development (14%); preservation of the environment (11%); agricultural, fisheries and forestry products (8%). 'administration' and 'other technical support' accounted for 17% of public funds invested in LEADER II.

LEADER+ (2000-2006)

The objective of the new initiative is to continue to encourage, on the basis of local partnerships, the emergence of, and experimentation with, rural territorial development strategies that are integrated and in a pilot form. These new models of rural development would be disseminated and would increase their value through a significant level of networking (EC, 1999). The LEADER+ initiative is exclusively financed from the EAGGF and is applicable to all rural areas of the Community with particular concentration on those areas, which demonstrate a real willingness and capacity to experiment with new and original forms of territorial development. The new initiative has three strands:

- Support for integrated development strategies of a pilot nature for rural territories relying on the bottom-up and the horizontal partnership.
- Co-operation between rural areas, both inter-territorial and trans-national dimension; and
- Creation of networks of actors.

Under the 2000-2006 LEADER programme in Ireland 38 LAGs were funded and are operational – giving an almost 100% coverage of all rural areas in the country. The total public funding (EC and Irish Government) amounts to EUR 150 m. About 45% of the funding for LEADER groups is provided from the budget for Ireland's National Development Plan (2000-2006).

Lessons from the EU LEADER experience

Strategies for rural development that have an area-based/spatial element and a 'bottom-up' method of implementation are now perceived as essential in complementing and reinforcing the traditional range of national macro-economic and structural policy instruments of development (OECD, 1996). The European Commission, through its policies, programmes and initiatives, has implemented with Member States, measures with a regional and bottom-up dimension. This is particularly the case of the Community's LEADER Initiative which emphasises partnership, a large participation of citizens and people's capacity building. Given the territorial and multisectoral dimension of rural development, the LEADER groups are generally comprised of actors representing the public, private and voluntary sectors.

The experience and lessons from LEADER indicate that the key elements of a local development approach are: an area-based rather than a sectoral development strategy; a competent local action group (LAG) to develop and manage the area-based development programme; a LAG that is representative; democratic and accountable; a LAG which places a high value on linkages and networks; a major emphasis on measures, which enhance the capacity of people and institutions at the local level to manage their own development; and a strong emphasis on innovation and adding value to top-down and sectoral approaches. The experience and lessons from LEADER under each of these headings are highlighted.

The area-based approach

The area-based, bottom-up approach of LEADER is an alternative to the traditional top-down forms of policy making. It allows for the identification of desirable policy measures through the consultation of relevant interest groups at the local level. Rural areas have a different set of resources and have different problems to resolve; measures adapted to each case are required. Centralised decision-making becomes inappropriate or insufficient as it cannot be adapted to take into account the

particularities of each area. LEADER has promoted and encouraged participatory decision-making which can ensure, insofar as it functions efficiently, a wide and fair representation of all groups of interest, thus creating an occasion for building up a consensus, dealing with conflicts and fostering interrelationships between sectors and groups.

Saraceno *et al.* (1999, p. 13) highlighted the importance of local involvement by saying that the design of development policies at local level may turn out to be more effective and manageable as it allows for the mobilisation of local resources (physical, environmental, cultural, human, economic, financial, institutional and administrative). The experience from LEADER indicates that the greater the depth of involvement, ownership and control by local communities, the higher the level of innovativeness in the projects implemented to tackle the development problems in the areas in question.

LEADER in Ireland has clearly recognised this rural diversity and has fostered a culture, whereby local people are encouraged to develop and exploit indigenous and unique resources. This approach adds value and mobilises previously underestimated or under-utilised resources. In Ireland, LEADER has mobilised large numbers of people (almost two-thirds of the national population) and harnessed local voluntary effort in a manner which could not be achieved through any other initiative. The value of the huge voluntary input arising from widespread participation means that the LEADER programme provides excellent value for money, leveraging at least twice as much private investment as that obtained from public funding.

Local groups - partnerships

The local action groups (LAGs) approved in the framework of LEADER, more often than not, reflect the way in which the national, regional and local authorities in each of the Union's Member States view rural development. However, the outstanding feature of the LEADER groups which have been most innovative and successful in multisectoral area development is the extent to which they have succeeded in getting meaningful involvement of a range of representatives covering the main sectors of economic and social activity in the rural area. Broadly, these include: the local community (elected representatives and community leaders); statutory/sectoral agencies; and the business sector.

The single greatest strength of the bottom-up approach is its potential to bring a new dynamism to local development. Where it has been successful, this has been achieved through harnessing community spirit, idealism and pragmatism towards what is necessary and possible to achieve locally, in partnership with national and local government agencies and the private/business sector.

The evidence from the LEADER programme in Ireland is that the LAGs, established and facilitated by the LEADER programme, now have the professional capacity to develop and implement innovative measures within the natural areas of development. The level of commitment and voluntary effort going into these groups is tremendous. The collective effort of voluntary board and staff together has proven to be a highly effective model for local rural development (Comhar LEADER na hEireann, 1999, p. 8).

Representation, accountability and democratic legitimacy

To achieve actual economic development at a small community level requires a genuine and effective partnership approach to development, local solutions which actively involve the private and voluntary sectors, public bodies and individuals, as well as democratically elected representatives. The LEADER LAGs represent such a partnership approach. However, for area-based development to be sustainable, partnerships must be perceived as having democratic legitimacy and accountability both by their local constituencies and by central authorities (EU, national, regional and local levels).

The 1996 OECD Report on local partnerships in Ireland, while recognising that the partnerships are 'extraordinary innovative', concludes that they have been better at creating new actions than at building stable institutions. The particular problem hinges around the fragile democratic legitimacy of the area-based partnership and their accountability to local constituencies and to central authorities.

At the heart of improving accountability is the matter of clarifying and co-ordinating what the connections should be between local partnerships, local and regional government and national agencies. How the co-ordination and connections can best be achieved will depend on the traditions and realities in relation to the administrative structures of national, regional and local government in Member States. However, two issues need attention in relation to the bottom-up/partnership approach. There must be a co-ordinating agency/mechanism in order to prevent duplication of activities and to improve legitimacy and accountability. Incremental reform in government agencies and their functions may be necessary to improve the level of responsiveness to bottom-up initiatives (Mannion, 1996, p. 4).

Subsidiary or decentralisation of responsibilities is critical to local area planning. LEADER in Ireland has succeeded in building institutional capacity at local community level, that has had a huge influence on the process of local government reform in Ireland. The enhanced capacity and organisation of communities has also resulted in the recognition of the importance of involvement of the community and voluntary sectors in local planning. This success is now set to be built on through new structures, known as County or City Development Boards (CDBs), which have recently been established in every county and city in Ireland. CDBs are bringing together, for the first time, the key players at local level to engage in a process of long-term planning for each county or city for the next ten years. The Boards are representative of local government, local development bodies (Area Partnerships, LEADER groups, and county/city enterprise boards) and the state agencies and social partners (employers and business, farming, trade union and community voluntary sectors) operating locally.

Linkages

The name LEADER explicitly states that actions and projects both within and between LEADER groups should not be individual and separated measures, but should be co-ordinated and well integrated where possible.

This is so as the predominant flow of public funds (EU and national) potentially available for rural areas follows a sectoral rather than an area-based route. This highlights the importance of linkages, inter-relationships and getting the balance right. Recognising the significance of sectoral funding in the context of its potential support for enterprise and employment in rural areas and the comparative limited role that area-based approaches, such as LEADER, can play in directly doing likewise is critical. Area-based partnerships have the potential to be the central cog that links/connects local needs and priorities with the sectoral cogs (sectoral programmes, funding and related agencies), which can supply the energy necessary for balanced and sustainable rural development. Without this

linkage LEADER groups and partnership companies can only make a limited contribution to achieving the goal of multi-sectoral development and a stable rural population.

Networking and transnational co-operation provided the framework for the exchange of information and experiences among all those involved in rural development actions. LEADER has set up many ways of networking and exchanging information, including:

- The LEADER Observatory which facilitates the exchange of experience at European level.
- National co-ordination units which have been set up in most of the EU countries.
- Transnational co-operation between LAGs from several Member States (Saraceno *et al.*, 1999, p. 28).

The Irish LEADER Network – Comhar LEADER na hEireann – was established in 1992 in response to the needs expressed by the local LEADER groups. The Network has played a vital role in training, facilitating interaction and exchange of information between groups, setting up best practice models and computerised records for the local action groups (Comhar LEADER na hEireann, 1997, p. 2).

Capacity building

Capacity building has become one of the most important functions of the LEADER programme, it developed the capacity and ability of the target population to participate in their own development and that of their community. It can even be said that the degree of success of this capacity building will be decisive for the success of the bottom-up approach to development as a whole.

What is it?

Local development capacity building means strengthening the knowledge, skills and attitudes of people so that they can establish and sustain their area's development. People create and adapt local institutions. It is people who create and shape the policies and measures which support their area's development. Changing institutional structures or policy measures without equipping people to manage and implement them is inadequate. Similarly, equipping management and field personnel (*e.g.* project staff) in the absence of support structures and conditions is inadequate.

Who is it for?

Capacity building, is necessary for all those involved in establishing and sustaining development in a rural area. It includes the individuals and groups in the target area, and the key persons working within the institutional environment, be they front line service providers or managers, and the decision-makers who support them (in the context of local action groups and other bodies responsible for implementing the LEADER programme, this is of particular importance). Also concerned are national, regional and local government agency representatives who have to see their role as 'partners' not 'power-brokers' at the partnership table. This implies new attitudes and a new type of capacity building. Their previous experience mainly relates to managing and implementing top-down and sectorally focused development initiatives. A considerable amount of re-learning is necessary if they are to successfully implement the bottom-up partnership approach.

Conventional capacity building has been mainly about skills training for project holders and the staff of development agencies. But the knowledge, skills and attitudes required to implement the

bottom-up model of local development differ considerably from that of being in control of service delivery on a territorial basis.

Capacity building for the progressive sector is easy. Conventional methods of stimulating interest and response are sufficient. Capacity building for the less progressive and the 'rural disillusioned' (*e.g.* rural youth) requires a different response from local development support agencies. This is particularly the case in rural areas, where the pre-existing level of local organisation is low. It also applies to economically marginalized rural areas, where the residual population may be apathetic and defeatist in attitude.

Particular emphasis needs to be placed on developing the capacity of these people to realistically appraise how their area may be able to provide the quality of life to which they aspire, and how they can be meaningfully involved in shaping its development. The educational and training institutions at all levels (primary, secondary, tertiary and adult) have a major responsibility in ensuring that rural people have the capacities and the skills necessary to contribute and be rewarded for the development of their own community.

Like development as a whole, building people's local development capacity is a slow process. Elected officials, European, national, regional, local decision-makers and "development activists" must be aware of this and support a long-term approach, despite frequent pressure to show immediate and visible results that are usually short-lived.

Innovation

The bottom-up and partnership approach advocated by LEADER is a novel, if not bold, experiment in making EU and Member State rural development policy more sensitive to local conditions. One of the aims of LEADER was to stimulate innovative measures in all sectors of rural activity. Since 1992 LEADER in Ireland has been innovative in its structure; programmes; training; capacity building and in the enterprises and projects it has supported. It offered rural areas new ways to plan and manage their economic and social development. It provided vital support both financial and advisory which enabled many creative ideas to be turned into successful business ventures.

Comhar LEADER na hEireann (1999, p. 9) concluded that the encouragement of innovation within the LEADER programme has enabled local groups to develop the type of creative responses to local issues which mainstream structure could not permit - 'a local solution to a local problem'.

LEADER groups are often the initiators of local development activities in rural areas. In addition, they act as key catalysts increasing co-ordination of activity between local agencies, thus, increasing the efficiency of local service delivery and maximising the use of financial, physical and human resources. Through their work they pilot models of development some of which can be mainstreamed. By their proactive initiatives, LEADER groups motivate others and create an impetus for other agents of development to act.

Part 3. Potential of the LEADER approach for the Baltic countries

The potential contribution of the LEADER approach, as a key component of a rural policy framework for the Baltic countries, is best understood within the context of the European Model of Agriculture and the 'Living Countryside' agenda, which was presented in Part 1 of this paper. Apart from the Common Agricultural Policy (CAP), the LEADER initiative has had most significant impact on the rural-based populations of many EU Member States. It has proven to be an important stimulus in rural areas that were lagging behind. However, it should not be viewed as a 'quick-fix' for the problems of rural decline, but rather as a long-term investment in building the capacity for development – particularly where community and local institutional confidence and capability has been seriously eroded. This has been the Irish experience. It is important to note that without a set of other farm and non-farm policy instruments, which enable the *broadening*, *deepening* and *re-grounding* of the role of farming/rural areas in the Baltic countries, the LEADER approach will not deliver its full potential.

The important positive aspects of the area-based approach as evidenced in the LEADER programme are that it:

- Complements and reinforces traditional economic and structural adjustment policies.
- Provides the basis for an integrated and holistic approach to development and maximises the use of resources (human, social, institutional and financial).
- Integrates what is being developed with the wider context of regional, national and European strategies.
- Recognises the diversity of rural areas and their differing needs.
- Increases the opportunities for citizen participation in their own development and deepens democracy.
- Brings a new dynamism to local development through harnessing community spirit and stimulated partnerships with national and local government agencies and the private business sector.

The success of the LEADER programme to date is due to the adherence to a number of important principles. These are:

1. A process of inclusion which involves the widest possible participation of citizens in identifying and tackling local needs and generating local solutions for local development.
2. A partnership structure to manage local development that is representative, democratic and accountable and that has the capacity to be innovative and successful in stimulating multi-sectoral local development.
3. An institutional framework for rural development that is built on the partnership principle to enable the bottom-up approach to be the mainspring of rural development policy strategy. It is the key principle necessary to ensure that there are strong vertical and horizontal linkages between the bottom-up approach and sectorally driven policies which impact on rural areas.

4. A real commitment to capacity building as the keystone of inclusive local development by the Commission, Member States and local development groups/agencies. This commitment must give recognition to the fact that capacity building: takes time; is people intensive; and requires resources. The rural development policy and the programmes and initiatives which are supported through it, must ensure that capacity building measures are included, resourced and implemented. This includes improving the capabilities of the institutions, which impact on rural development, as well as the skills of those who work for, or direct, the activities of such institutions.

These are key principles which the Baltic countries need to fully understand and take into account should they choose to follow an area-based LEADER style approach as part of an overall rural renewal strategy.

The bottom-up approach as implemented in the LEADER Community Initiative should become one of the mainsprings of European rural policy for the Baltic countries. Development strategies based on this approach help ensure cohesion and coherence between agricultural and rural development policies. There are obvious risks attached to empowering local communities, particularly for those who have to share power, but this may well be the price that has to be paid to have a more socially inclusive Europe, where farm and non-farm rural households have a meaningful input to decisions that impact on their living standards.

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RURAL AND REGIONAL DEVELOPMENT POLICY IN ESTONIA

By Ms. Riin Saluveer

Abstract

This paper reviews Estonia's rural and regional development policies, gives an overview of the current administrative division, rural and regional development policy objectives and instruments in light of EU accession. The main institutions influencing rural and regional development in Estonia are the key ministries (the Ministry of Internal Affairs, the Ministry responsible for Regional Affairs, and the Ministry of Agriculture), as well as the local and county governments. Rural and regional development policies are influenced by the possible accession of Estonia to the EU, therefore besides the national scheme on rural and agricultural development supports, the pre-accession instrument SAPARD is targeted to fulfilling the policy objectives. With regards to EU accession, Estonia will become Objective 1 area. In order to become eligible for support under EU Structural Funds and the EAGGF Guarantee Fund, Estonia is preparing two programme documents: Single Programming Document 2004-2006 and Rural Development Plan 2004-2006, which set the strategy, priorities, objectives, and instruments for the allocation of EU funds in Estonia.

Background

Estonia re-gained independence in 1991. Since then, there have been substantial changes and deep restructuring in the developments of the agricultural sector and rural areas, from soviet-type purely agricultural collective farm oriented rural society to diverse rural development and market oriented agricultural entrepreneurship. The command economy has changed to the market economy. Most enterprises in the primary agricultural sector and processing sector are already privatised, and land reform has been carried out. Changes in the economic environment in the 1990s resulted in a lower employment rate in the agricultural sector, and high structural unemployment (qualified work force is not available for vacant jobs), which rendered rural areas unattractive for people in terms of work and self-actualisation.

The large migration of younger and more educated people from rural to urban areas in the 1990s has impaired the human potential of rural areas and reduced the availability of a skilled work force and the quality of the work force. Compared to urban areas, Estonia's rural areas are characterised by sparse population and high average age, low purchasing power, and closed local communities in some places. The changing market situation and reforms have reduced the relative share of agriculture in the national economy, employment, and land use, which has resulted in great changes in the landscape; *e.g.* the amount of abandoned land has increased substantially.

The regional differences have grown since the 1990s. Various disparities are striking when one compares the capital city region (Tallinn and Harju County) and other parts of Estonia (SPD 2003). Harju County, accommodates 40% of Estonia's population and gives 60% of GDP and 80% of foreign investments. The GDP per capita in Harju is approximately 51% of the EU average, while the respective indicator in other counties remains between 22-25%. Among other counties the most successful are Tartu and Pärnu with strong town centres. The situation is least favourable in counties located on the eastern border (with the exception of Tartu County). Ida-Viru County is also rather special, being the only industrial region suffering from adaptation difficulties. In other counties, the

difficulties are mostly related to the decline of agriculture, made more complicated by different local factors and characteristics.

Regional disparities increased over the transition period and have started to have some effect on the migration of the population. Economic and social motives cause young people to choose bigger towns, especially Tallinn. Such a trend is somewhat offset by the movement of elderly people from towns with high residential costs to rural areas. This type of migration has increased by approximately 40%, compared to the Soviet period. The towns have also become dominant. Approximately 1/3 of the labour force living in rural areas has jobs in towns and cities.

Administrative regional division

The government structure has three levels: the Government of the Republic, county governments and local governments. There are 15 counties led by the county governors (county governors are appointed by the parliament - *Riigikogu* - at the proposal of the Government). The latest data in 2003, indicates that there were 39 self-governed towns and cities and 202 rural municipalities. There were 4 610 settlements in rural municipalities, including 8 cities and 6 towns without municipal status, 172 small towns and 4 424 villages.

Rural population in Estonia

In Estonia, the relative share of the urban population is 67.4% (2002). The population system is dominated by the capital city – in 2002, 398 000 inhabitants lived in Tallinn. Approximately 40% of Estonia's population lives in Tallinn and its surrounding area (Harju County). The second largest town – Tartu (101 000 inhabitants) – is the regional centre for six counties. The largest towns of Ida-Virumaa – Narva (68 000 inhabitants) and Kohtla-Järve (47 000 inhabitants) – are industrial towns that provide rather weak central functions for the surrounding areas. Pärnu (45 000 inhabitants) is an important resort town. The remaining 35 towns, some of which also perform the tasks and functions of a county centre, are relatively small (1 000 – 20 000 inhabitants).

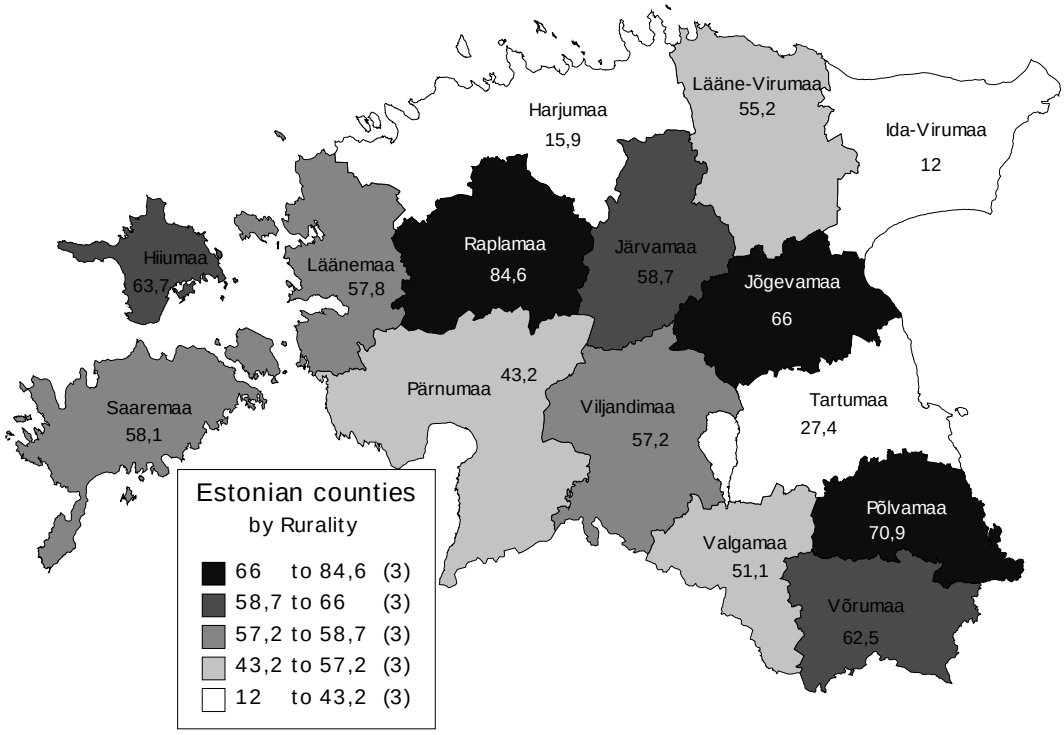
Definition of rural areas in Estonia

The most widely used definition of rural areas is according to the administrative distribution, which divides the local governments in Estonia into rural municipalities and urban municipalities (towns). This division is also used in the statistics, but the problems arise from the administrative reform during which some municipalities with different status have merged.

In some other cases, additional definitions are used for specific purposes, for example, in the national Regional Development Strategy (1999), the rural areas are defined as the areas outside cities with over 2 500 inhabitants. In the Rural Life and Agricultural Markets Organisation Act that sets the basis for agricultural support systems, the rural area is the area of the village, borough and townlet, and this definition roughly corresponds with the definition of the statistical office.

According to the definition by administrative distribution, on average, 33% of the Estonian population lives outside towns. It must be emphasized that some of the towns in Estonia are quite small, the smallest with approximately 1 500 inhabitants. Map 1 shows the percentage of the rural population compared to total population in counties.

Map 1. Percentage of rural inhabitants out of total inhabitants per county, 1 January 2002

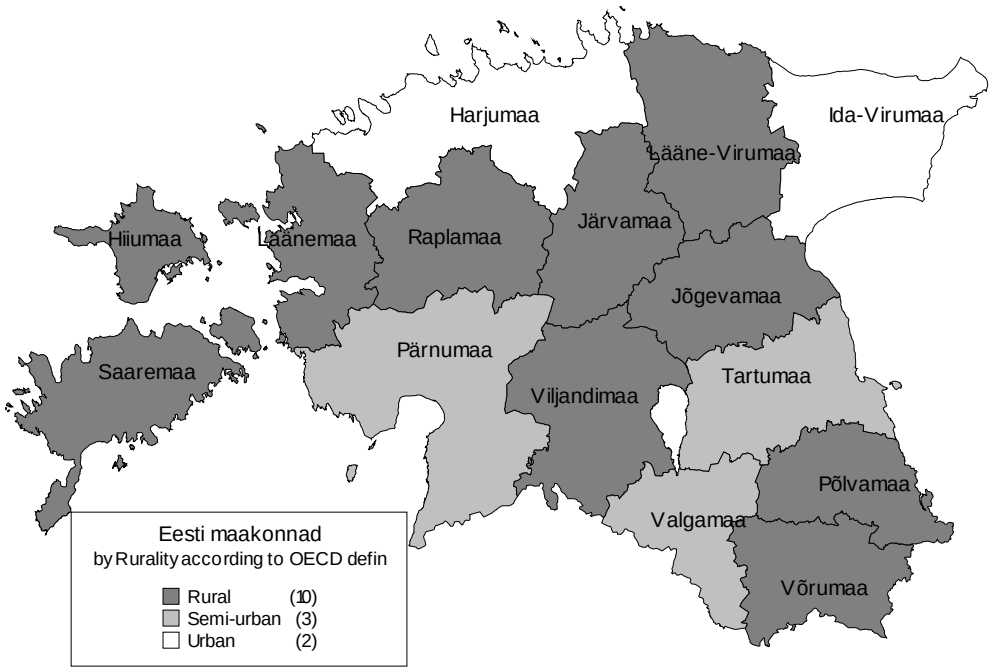


Source: Regional Statistics of Estonia 2001, Statistical Office of Estonia, Tallinn 2002 (ESA 2002).

OECD's definition of rurality applies population density as the main criteria for defining rurality, dividing regions into urban, semi-urban and rural areas. Estonia is quite sparsely populated compared to EU countries, the average population density in Estonia is 33 inhabitants per km^2, and for rural areas even much lower – in 1/3 of rural municipalities it is even below 8 in/km^2 (Map 2).

According to this criterion, Harjumaa and Ida-Virumaa would be urban, semi-urban would be Pärnumaa and Tartumaa and Valgamaa and all the other counties fall into the rural category.

Map 2. Rural areas in Estonia



Institutions influencing rural and regional development policies

The main institutions, whose policy is targeted directly for the rural and regional development, are the Ministry of Agriculture, Ministry of Internal Affairs, Minister responsible for Regional Affairs, County Governments and Rural Municipalities. All other ministries that are carrying out sectoral policies (Ministry of Social Affairs, Ministry of Economy and Communication, Ministry of Culture etc.), also target, to a smaller or larger extent, the development of rural areas, with policies being still more horizontal.

The Ministry of Agriculture is responsible for making proposals and implementation of agricultural and rural policies in Estonia. The main fields of activity of the Rural Development Department in the Ministry of Agriculture are the rural entrepreneurship, living environment of rural areas, infrastructure and land amelioration, forestry, extension, science and training activities.

The Department of Regional Development and the Department of Local Government in the Ministry of Internal Affairs are responsible for the overall co-ordination of issues of local government and regional development, analysing, planning and co-ordinating the country's local government and regional development policy within its competence, assist the establishment of links between local authorities and their associations and the government, deal with county government issues, except for the assessment of the justification of the structures and compositions, arranging the administrative division of the state territory and co-ordinating and implementing international co-operation programmes and foreign aid projects for local government and regional development.

Rural development policy

During the period 1999-2003, Estonia's agricultural and rural development policy was heavily influenced by the preparations of Estonia's accession to the European Union, with the main keywords being the harmonisation of the legislation and adaptation of the agricultural sector to the conditions in the EU. The strategy for the development of agriculture (2000) launched in 1999 set the objectives of agricultural policy for the pre-accession period, as well as the measures for achieving them for the period 2000-2003. The main objectives were, besides those targeting the agricultural sector, the development of rural economy and development of agri-environmental programmes.

In 2003, Estonia is implementing several types of national rural and agricultural supports, which have been developed since their introduction in 1992, with indirect support measures. In addition, since 2001, supports in the framework of EU pre-accession instrument for agriculture and rural development - SAPARD – were launched, which contribute to the adaptation of the agricultural and rural sector in the light of Estonian accession to the EU.

National supports

The national budget has a separate budget line for agricultural and rural development support schemes, which is discussed with the social partners and decided on how to allocate it. The agricultural development strategy set several support measures for achieving its objectives, for which the legislative basis was given with the Rural Development and Agricultural Market Regulation Act (RT I 2000, 82, 526) that came into force at the end of 2000. This Act provides state measures for the balanced development of the market for agricultural products, the profitability of production of agricultural produce, and the development of other rural economic activities. The classes of state support granted on the basis of the Act are as follows: development support, income support, market price support and school milk support. The development support could be investment support for agricultural production, investment support for the processing of agricultural produce, investment support for rural enterprises, investment support for the development of rural infrastructure and the living environment in rural areas, investment support for young entrepreneurs starting agricultural production, interest support, agricultural insurance support, advisory support, training support, practical training support, support for the liming of agricultural land, agri-environmental support, joint economic activity support for agricultural producers and market development support. Several development measures are targeted to the technical support for the agricultural producers or rural entrepreneurs with the objective of increasing competitiveness of the sector – such as training support or advisory support. Environmental aspects have become very important, for example, the investment measures are targeted to environmental investments in farms, and also agri-environmental measures have been elaborated since 1999.

Agri-environment

The development of agri-environmental measures and the necessary administrative structure has been underway in Estonia since 1999. The objectives of the agri-environment support are to enhance environmentally friendly agricultural production, maintenance of natural or cultural values and landscape elements, illustrating the landscape or establishment of new landscape elements. The following activities qualified for agri-environmental support in 2002:

- Use of methods for good plant production practice.
- Environmentally-friendly management.

- Organic farming.
- Growing local endangered breeds.
- Restoration and maintenance of stonewalls.
- Establishment and maintenance of mixed species hedgerows.
- Establishment and maintenance of ponds and wetlands.
- Maintenance of temporary set aside arable land covered with brushwood.
- Maintenance of temporary set aside arable state land, which is not covered with brushwood.

In 2003, the support is financed from the state budget within the same scheme and areas as in 2002. However, as the pilot schemes are designed to test the practical implementation of proposals for a national agri-environment programme and to identify potential problems with application and control procedures, changes to the regulations were made in early 2003.

The practical experiences acquired from the implementation of measures in the pilot areas in 2001 allow the development of agri-environment measures satisfying the requirements of the Council Regulation 1257/99/EC and the respective administrative capacity.

Other measures

Practical support is given to the agricultural producer, who provides internship for students specializing in agriculture. **Training support** is given to agricultural producers, fishermen, small-scale processing entrepreneurs, or handicraft entrepreneurs for covering the expenditure for training, which is targeted to the acquisition of necessary skills for economic activities. **Support for common economic activity** is a support scheme established in 2001. The support could be applied to partly compensate the foundation and running costs of profit co-operatives. The members of profit co-operatives must include at least 5 agricultural producers, professional fishermen or fish producers and the co-operative itself oriented to marketing or processing of agricultural produce or fish, sale of agricultural or fish products or capital or floating assets needed in agricultural or fish production. **Advisory support** could be applied by agricultural and fish producers having procured agricultural advisory service from an accredited consultant of agriculture or rural development.

SAPARD programme

The pre-accession agriculture and rural development instrument SAPARD was introduced to Estonia in 2001, when the first four measures were accredited. The main objective of the programme is to contribute to the implementation of the "*acquis communautaire*", concerning the common agricultural policy and related policies and to solve priority and specific problems for the sustainable adaptation of the agricultural sector and rural areas in Estonia (RDP 2000). More than EEK 250 MEEK per year are channelled to agriculture and rural development sectors in the framework of the SAPARD programme. About 75% is financed by the European Union and 25% by Estonia. The programme co-finances up to 50% of the costs of investments. In the first years, the money from the programme is distributed between 4 different types of investment supports:

- Investment support for agricultural production (measure no. 1).

- Investment support for processing and marketing of agricultural and fishery products (measure 2).

- Investment support for development and diversification of alternative economic activities in rural areas (measure no. 3).

- Investment support for rural infrastructure (measure no. 4).

Within the SAPARD programme the measures for technical assistance (measure no. 5) and measure for the regeneration and development of villages (measure no. 6) will be launched in 2003. Two other measures were also described in the programme – agri-environmental measures and afforestation measures – which will presumably transfer to the post-accession measures without being implemented within the SAPARD programme.

One of the side-objectives of the pre-accession instrument is the development of institutional capacity for administering the common agricultural policy and related policies after Estonian accession to EU. Supports of the SAPARD-programme are administrated by the Agricultural Registers and Information Board (ARIB), which has been accredited as SAPARD Paying Agency and will operate as a Paying Agency for EAGGF supports after the accession.

Investment support for agricultural production (measure no. 1)

The long-term objective of the measure is to support the agricultural sector in meeting its commitments related to implementation of EU legislation and policies (*acquis communitaire*), but also to use rural diversification as a tool stabilising rural economy and maintaining jobs in rural areas (RDP 2000). During the implementation of the measure, support is given for the following investments (ARIB 2003):

1. Investments aimed at bringing agricultural production into conformity with different European Union requirements, including investments in milk production technologies matching EU veterinary and hygiene requirements aimed at increasing the share of milk meeting minimum EU requirements, and investments in barns meeting animal welfare and environmental requirements and investments in crop protection, seed propagation and organic fertilizer spreading technologies, to meet the phyto-sanitary and environmental requirements.

2. Investments aimed at diversification of agricultural production, including investments in certified or controlled plant propagation materials for orchards and berry plantations and plant propagation materials for open-grown ornamental trees and plant plantations and purchase of machinery and equipment, irrigation and fertilisation machinery and equipment and enclosures and constructions for new orchards, berry plantations and open-grown ornamental trees and plant plantations and purchase of objects of apiculture.

Investment support for processing and marketing of agricultural and fishery products (measure no. 2)

The purpose of this measure is to contribute to the implementation of the "*acquis communautaire"* contributing to the common agricultural policy and related policies, focusing on specific problems of processing industry. In implementation of the measure, support will be granted to investments for product development, marketing and product quality improvement, bringing processing facilities in conformity with relevant EU standards. Investment support is given for dairy processing, meat processing and fish processing.

Investment support for development and diversification of alternative economic activities in rural areas (measure no. 3)

The objective of this measure is to contribute to solving problems related to the abrupt fall in employment rates in rural areas and sustainable conversion of the rural areas in Estonia, accompanied by increased employment opportunities. The measure is also intended to support activities based on local initiatives, supporting establishment of diversified economic activities in rural areas, creation of additional jobs that provide for additional income. Investment support is given for the following activities: rural tourism and related activities, handicraft activities, service enterprises (*e.g.* purchase of agricultural and forest machinery, storage facilities, special equipment services necessary for local inhabitants, construction and renovation of buildings required for listed service activities, child-care facilities, youth-centres, alms-houses, nursing homes), crayfish and fish farming and food processing in small enterprises.

Investment support for rural infrastructure (measure no. 4)

The general purpose of this specific measure is to solve the priority and specific problems relating to the infrastructure of scattered settlements in rural areas. Investment support is given for electricity supply systems (purchasing equipment necessary for merging energy distribution network or reconstruction of electricity systems), access roads, water supply and sewage and telecommunications.

Investment support for regeneration and development of villages (measure no. 6)

The objective of this measure is to support the activities based on local initiatives, which improve the development of villages, increase the initiatives and co-operation between people and improve the overall quality of life in villages. Within the framework, support is given for building, reconstructing and furnishing buildings open to the public, which are related to the common activities of the village inhabitants or development of village culture or preserving of environmental values. The measure is expected to be launched in 2003.

SAPARD programme progress

In order to assess the programme progress, it should be pointed out that the mid-term evaluation of the whole programme will be carried out during 2003, therefore it is too early to make too many conclusions at this stage. But, shortly it can be said that the programme progress has been satisfactory, and the second year of receiving applications was more successful when compared with that of 2001. Taking into account the three-year budget and a two-year SAPARD implementation, support has been applied in approximately 54% of cases, and 42% of the budget was approved. In total, 361 applications were approved in 2001-2002. The investment sum of these applications was 754 million EEK in total, and the amount of support was 317.5 million EEK. The second year of receiving applications was more successful when compared with 2001. The progress has been different for different measures. The second measure is the most used measure, where commitments are 95% of the budget. The finances for measure 1 have also been committed quite well, while measure 3 should be used more. Measure 4 is used less - under the measure, approximately 4% of applications are approved. In order to improve the situation, the Ministry of Agriculture has held discussions with the social partners and has already made some changes to the measures and relevant legislation. Several aspects have been changed, which have been regarded as obstacles in applying for support, therefore, the situation should improve in 2003.

Regional development policy

The Estonian Government carries out the general administration of regional policy. The Minister responsible for Regional Affairs is responsible for the implementation of regional policy. Ministries are responsible for impacts of the activities on regional development under their jurisdiction within the limits of the tasks set on them. The Minister responsible for Regional Affairs and the Ministry of Internal Affairs co-ordinate the regional policy of Estonia as a whole.

The **Strategy for Regional Development** (1999) includes a well-defined nomenclature for programmes and target areas. The long-term goal of Estonian regional policy is to secure a high quality of life for the country's population. This is to be achieved by strengthening and ensuring the maximum use of local preconditions for development, which contribute to the general macroeconomic and social development of the state (Overview of Estonian Regional Policy).

A wide range of policy instruments are in place, including:

- Local public transport subsidies.
- Organization and subsidies for transport and communication services between the mainland and the islands.
- Regional development programmes.
- Business promotion centres.
- Development fund for county governments.
- Support programme for regional investments in social infrastructure.

According to the Regional Development Strategy, one of the main components of the regional development policy of Estonia is regional development policy directed to target areas, which is implemented in the form of regional development programmes in specific target areas. Measures of regional development programmes are intended for the development of human resources, business activities and infrastructure. Seven regional development programmes are functioning during the period, before accession to the European Union:

- Programme for the Islands.
- Programme for the Areas of Agricultural Restructuring.
- Programme for the Areas of Industrial Structuring.
- Programme for the Network of Centres.
- Programme for the Setomaa Region.
- Programme for the Local Initiative.
- Programme for Cross-Border Co-operation.

The **Estonian Regional Development Agency** acts as a fund manager for the majority of the instruments of national regional policy. The main areas of activity of the agency are in respect of regional development programmes organising utilisation of the funds prescribed for regional development programmes, co-ordinating the work of regional development programmes and auditing the utilisation of the funds allocated by programmes. In respect of the enterprise support system, ERDA is developing and furthering an effective system of enterprise counselling on the basis of enterprise centres and business advisory centres, co-ordinating activities and exchange of information of the business advisory centres and enterprise centres, which belong to the enterprise support system; developing an information system, developing new measures designed for developing business and organising training for the staffs of enterprise centres and business advisory centres. ERDA also organises research concerning regional development and participates in projects financed by the European Union.

According to the assessment made for the regional development projects in Estonia (A*ssessment of the results…2001),* the general conclusion was that, in principle, the regional policy through projects is working – there are good projects, but the share of those and the results must be higher. There are projects, which have well profited from local prerequisites for development, and which have clear results (*i.e.* as created jobs), and where the original solutions have been used, but those kinds of projects are still a minority among the total. In order to improve the situation the priorities must be clarified, good practice (with regards to the applicability) must be spread out more and a pool of professional project leaders must be developed. The evaluators stressed also that it all needs the sustainability and stability of Estonian regional development policy.

EU instruments

The European Union has also influenced the regional development of Estonia besides the SAPARD programme, above all through a Phare Cross-Border Co-operation Programme - Phare CBC (SPD 2003). In 1994-2000, different regions in Estonia received assistance from Phare amounting to EUR 26 million (more than 400 million kroons), which is twice as much as the amounts received by Estonian development programmes for national regions. The target areas for cross-border co-operation in Estonia lie mostly outside Tallinn. However, they do not match the preferences established in the national programmes developed in Estonia. Considering the character of cross-border co-operation, this is inevitable. Since 2000, the preferences of national regional policy are being observed through the implementation of Phare social and economic cohesion investment funds. The ISPA support to investments made into transport infrastructures and environment protection is to improve the situation in the regions out of the capital city area.

Role of county governments and local governments in rural and regional development policies

On the regional and sub-regional level, the role of county governments and local governments in regional and rural development becomes evident.

County governments are government agencies, which represent the state in 15 regions in Estonia. County governments are currently responsible for the co-ordination of sectoral policy activities, like strategic planning, tourism and business development. The head of County governments are County governors, who represent the interests of the state in the county and care for the comprehensive and balanced development of the county, act as an intermediary between the state and local governments, guide and co-ordinate the work of regional offices of state, make proposals to the Government of the Republic for the management of the work of state agencies located in the county, possess, use and dispose of state assets; monitor the activities of local governments, make proposals to the Government of the Republic concerning the draft annual budget of expenditure and revenue of the

county government and ensure the purposeful use of funds, aid and grants allocated by the European Union, and other foreign aid (Government of the Republic Act).

The task of **local governments,** provided by law, is to organise the following: social welfare and related services, care for the elderly, youth work, housing and public utilities, water supply and sewage, property maintenance, territorial planning, public transport within a municipality or town, garbage collection and street cleaning in municipalities or towns. **The total amount of local budgets** was 10 933 billion kroons in 2001, amounting to 21.7% of the consolidated state budget. The main sources of income for a local budget are state taxes paid into local budgets (proportional share of personal income tax and land tax) and allocations from the state fund, supplemented by funding from a variety of sources.

The financial resources allocated from the state budget for supporting local budgets can be observed as replenishing and balancing the revenues of local budgets and national investment support to municipal investments.

While providing the basic services, local government units have very few **assets required for promoting local development activities** (local marketing, organisation of events with major economic impacts, promotion of information society, supporting voluntary development initiatives, business training and counselling, mobilisation of the unemployed, etc.). Capital for developing related structures (facilities, office sites for enterprises, industrial parks, etc.) is also in short supply. Limited funding can be obtained from different state-owned foundations, supplemented by mandatory municipal contributions.

All the local government units must have development plans and comprehensive plans for years to come. These documents serve as the basis for making decisions related to regional development, but the availability and quality of such documents is not ensured at the moment.

Policy measures regarding EU accession

After Estonia's accession to the European Union, which will presumably take place in 2004, Estonia will have to implement EU agricultural and structural policies. Estonia will become a region covered by Objective 1, which is described as "promoting the development and structural adjustment of regions whose development is lagging behind" and provides the largest support rates. Preparation for the post-accession activities already started at the end of 2001 with the programming of two framework documents for the period from 2004 to the end of 2006 (RDP 2003):

- The National Development Plan related to the implementation of Structural Fund measures.
- The Rural Development Plan, related to the implementation of Common Agricultural Policy measures.

Both plans continue the work which was started under the SAPARD programme, paying more attention to regional issues, which should help even out the disparities.

National Development Plan 2004-2006

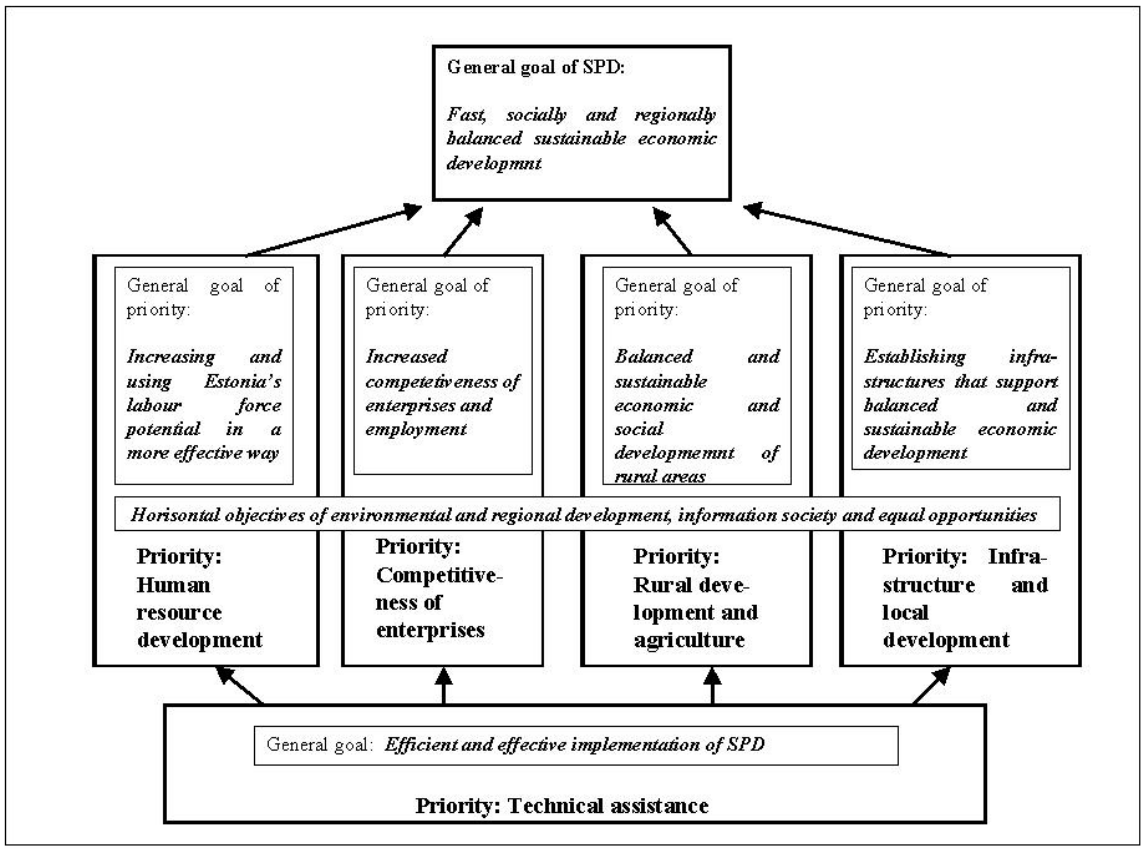
To become eligible for assistance from EU Structural Funds, Estonia must present a single programming document that covers a period of several years. The "Estonian National Development Plan for the Implementation of the EU Structural Funds – Single Programming Document 2003-2006" (SPD 2003) is submitted to the European Commission for approval.

The main objective of the National Development Programme is fast, socially and regionally balanced sustainable economic development. To achieve the prime objective of the Programme, Estonia will commit itself to four specific objectives. These are as follows:

- Increasing and using Estonia's labour force potential in a more effective way.
- Increased competitiveness of enterprises and employment.
- Balanced and sustainable economic and social development of rural areas.
- Establishing infrastructures that support sustainable and balanced economic development.

The four key priorities in the Single Programming Document are human resource development, competitiveness of enterprises, rural development, agriculture and infrastructure, and Local Development.

Chart 1. Goals and priorities of the Estonian Single Programming Document



Rural development and agriculture in SPD

Strengthening the economic basis for rural development will focus on increasing the competitiveness of the food production chain as a whole – from initial production to final processing – by providing support to investment projects. Alongside the modernisation of traditional agriculture, the priority will contribute to the diversification of agricultural production, development of product quality, improvement of the environmental situation, development of sustainable forestry and the creation of new non-agricultural enterprises and employment in the countryside. The opportunities related to the enhanced use of the local natural environment and cultural heritage will be addressed in the development of non-agricultural economic activities. The priority criteria for developing alternative economic activities is the creation of new jobs to provide employment for people leaving, or going to leave, agriculture and utilization of local resources – rural tourism, handicraft, etc. Besides direct investments into main production areas the priority will support the modernisation of agriculture and forestry by the maintenance of depreciated amelioration systems. Specialized counselling and advisory services aimed at improving the skills and knowledge of agricultural and forestry, as well as other rural economy entrepreneurs will be provided within the framework of this priority.

Reconstruction or construction of buildings intended for public use, but also development and implementation of local partnership-based pilot development strategies – SPD has integrated the measures that are applicable within the LEADER initiative – will be supported to make the living environment in villages more attractive. The activities will positively affect the level of local initiative and viability of rural areas.

As for fisheries, the aim is to reduce the fishing fleet with excessive fishing capacities and provide retraining opportunities for the fishermen who have lost their jobs. The focus will be targeted to the investments necessary for bringing all the links in the fish-handling chain (vessels, ports, industries) into conformity with food safety, occupational safety and environment protection requirements. Establishment of fish and crayfish farms will also be supported to compensate for the decrease in the fishing capacity and diversify the economic basis of rural life. The marketing of fish products will be facilitated to improve access to markets.

During the implementation of this priority the co-ordination with other priorities, especially with infrastructure and local development priority, as long as the living and business environment both in the urban and rural areas is largely shaped by the nature and availability of infrastructures provided by the state and local municipalities.

The implementation of the priority will be funded by two structural funds – Guidance section of the European Agricultural Guarantee and Guidance Fund (EAGGF) and FIFG (fisheries). The priority's relative weighting for the implementation of the Programme is about 20% of the total funding allocated for the SPD.

The following Table describes measures that will be implemented within the framework of Rural Development and Agriculture, both under EAGGF and FIFG, pointing out the differences between SAPARD and future structural funds:

Table 1. The measures implemented under the EAGGF and the FIFG

EAGGF	**Pre-accession instrument SAPARD**
Investment into Agricultural Holdings	Measure 1
Investment Support for Improving the Processing and Marketing of Agricultural Products	Measure 2
Diversification of Economic Activities in Rural Areas	Measure 3
Integrated Land Improvement	
Renovation and Development of Villages	Measure 6
Local initiative based Development Projects – LEADER	
Support for Provision of Advisory and Extension Services	
Forestry	
FIFG	
Investment Support for Aquaculture	(partly measure 3)
Investment Support for Processing and Marketing Aquaculture Products	(partly measure 2)
Promotion of New Market Outlets	
Modernisation of Fishing Ports	
Restructuring of the Fishing Fleet	

Infrastructure and local development

The priority of infrastructure and local development will cover several aspects of Estonian regional development policy during the pre-accession period, especially the measures contributing to local development.

In the context of infrastructure development, Estonia's strengths are related to road network and community infrastructure with a relatively good coverage, quite well-developed telecommunications networks and ICT services for public use. On the other hand, poor technical conditions of several buildings and facilities (mostly attributable to insufficient funding), non-compliance with modern technical safety requirements and environmental protection requirements, as well as the changing social and economic needs are the main weaknesses. Past pollution covering large areas is also considered to be a serious problem.

In order to achieve the prime objective of the Single Programming Document – to promote fast, socially and regionally balanced sustainable economic development – this priority concentrates on the development of those parts of the infrastructure that have direct impact on the socio-economic development, or the improvement of which cannot be postponed any further. Development of infrastructures held by private bodies will not be supported, as a rule. In general, no support will be available for commercial telephone and data communication networks, or the distribution of electricity and transmission networks.

Implementation of the infrastructure and local development priority will be co-financed under the European Regional Development Fund (ERDF).

The priority is implemented through the following seven measures:

- Information Society Development.
- Development of Local Living Environment.
- Increasing the Competitiveness of Regions.
- Development of Transport infrastructure.
- Development of Environmental infrastructure.
- Modernisation of Infrastructure for Vocational and Higher Education.
- Reorganisation of Hospital Network.

Two measures are of particular interest when considering the present-day regional development policy in Estonia: development of local living environment, and increasing the competitiveness of regions. The overall objective of the measure on development of local living environment is to contribute to Estonia's general sustainable and balanced economic development through the elimination of bottlenecks in local infrastructures. The specific objectives of the measure are improving and strengthening the investments supporting the programme through other measures, improving and unifying availability and quality of public services, energy conservation, regional improvements and the unification of human resources.

The overall objective of the measure is to increase the competitiveness of regions and to support general sustainable and balanced economic development in Estonia. Both measures include several types of activities – both investments and also development aid to different kinds of needs municipalities have in Estonia. For the transition from pre-accession policy to post-accession policy, it has to be mentioned, that several regional development programmes mentioned above exist in Estonia in 2003, and will later be co-financed by the EU, mainly under the measure for increasing the competitiveness of regions, with some exceptions.

Rural Development Plan 2004-2006

Support measures co-financed by the European Agricultural Guidance and Guarantee Fund (EAGGF) are of particular importance in view of rural development. The rural development measures financed from the EAGGF Guarantee Section that Estonia plans to implement upon accession to the EU are the following:

- Support to less-favoured areas and areas with environmental restrictions.
- Agri-environmental support (which is compulsory measure in EU member states).
- Afforestation.
- Support for semi-subsistence farming.
- Compliance with EU standards.
- Technical aid (supportive measure).

The RDP was prepared by the Ministry of Agriculture with the involvement of co-operation partners and specialists. The task of implementation of the RDP measures lies with the Ministry of Agriculture and the agencies within its area of administration; units of the area of administration of the Ministry of the Environment are involved in the implementation of the relevant measures.

However, the level of rural development plays an important role in improving the quality of life of the entire population. The greater opportunities of people (welfare) and their mobility boost the need for the natural and traditional cultural environment. The strategy set in the Rural Development Plan 2004-2006 presents the rural development vision, the bases and goals of rural policy and the measures for attaining these goals, based on the rural population and their needs. The specific goals of this strategy are:

- To preserve the rural environment and landscape.
- To alleviate the impact of the transitional problems that agriculture faces in the medium term.
- To support the regionally balanced functioning of rural areas.
- To diversify rural enterprise by improving the infrastructure and developing technologies with a view to the new quality and competition conditions.
- To promote environmentally friendly production methods that take account of cultural heritage.
- To contribute to the improvement in living standard in rural areas, while preserving a viable rural community.
- To support the change of generations and professional agricultural training.

In the situation described above, the purposeful and efficient implementation of the European agricultural policy and rural development measures, which are described in the Rural Development Plan and the rural development and local development priority of the National Development Plan, is essential to ensuring a balanced regional development in the entire country.

Conclusion

The main institutions in Estonia, whose policy objectives are directly linked to rural and regional development and regional cohesion, are the Ministry of Agriculture, Ministry of Internal Affairs, Minister of Regional Development, County Governments and Rural Municipalities, besides the sectoral ministries whose policies are more horizontal. Estonia's rural and regional development policies in 2003 are both influenced by Estonia's possible accession to the EU. The pre-accession agricultural and rural development instrument SAPARD, has been implemented since 2001, and has contributed to the adaptation of the agricultural sector and rural areas to the changes brought by Estonia's accession preparations to the EU. The regional development policy's main component is directed to target areas, which is implemented in the form of regional development programmes. In order to become eligible for support under EU Structural Funds and the EAGGF Guarantee Fund after Estonia's accession to EU, Estonia is preparing two programme documents: Single Programming Document 2004-2006 and Rural Development Plan 2004-2006, which set the strategy, priorities and objectives and instruments for the allocation of EU funds in Estonia.

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RURAL AND REGIONAL DEVELOPMENT IN LATVIA

By Mrs. Maija Dreimane, Ms. Ginta Uzulina, Ms. Ieva Simane, Mr. Janis Jurgis and Mr. Ritvars Zapereckis
(Paper presented by Ms. Marita Baltina)

Abstract

The objective of this report is to describe the policies of rural and regional development in Latvia, explaining the main problems in rural areas of different regions, as well as identifying the main instruments, which are used to achieve the effective development of rural areas, and regions. In Latvia several programmes are implemented, which are aimed at facilitating the economic development of rural areas by supporting agricultural and non-agricultural businesses, and improving the infrastructure. Besides, several instruments and programmes are used to improve regional development, which strongly influence the socio-economic conditions of rural areas. In this report the main advantages and weaknesses are outlined, in order to identify the future tasks for improving the effectiveness of rural and regional policies.

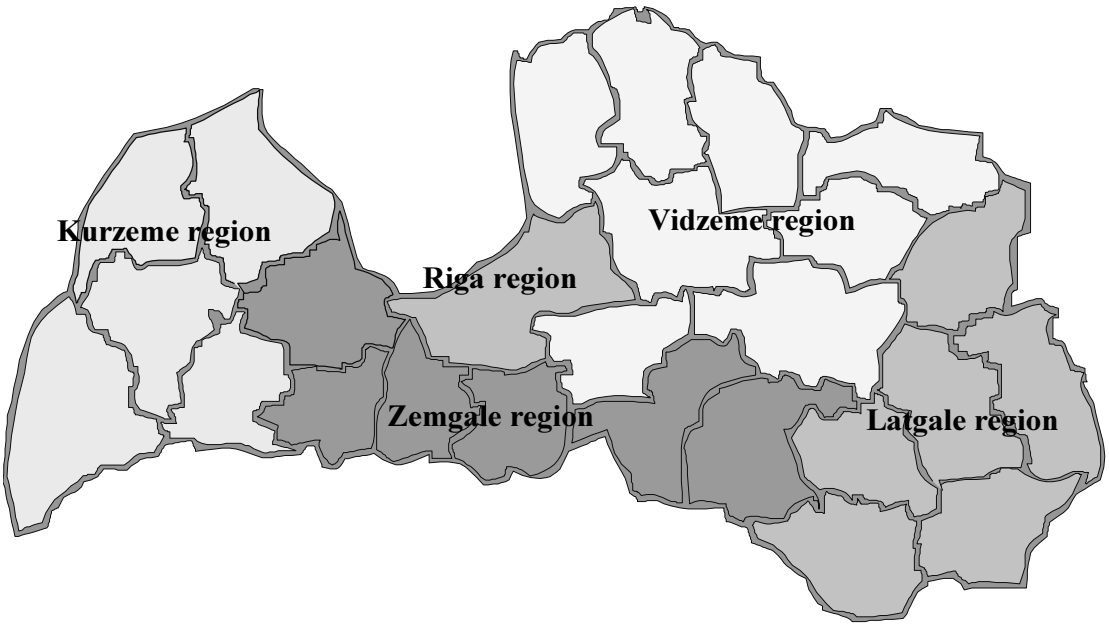
Description of rural and regional development

Regional development and description of regions in Latvia

Administratively, Latvia is divided into 33 regional local governments: 26 districts and seven cities, which in addition to the functions of territorial local governments also perform the functions of district local governments. Latvia has 547 territorial local governments, and at present, a merger of territorial local governments is taking place. The government has approved an indicative project for the establishment of 102 territorial local governments. The administrative territorial reform is taking place in Latvia and its objective is to increase the operational efficiency of local governments by creating local governments at several levels (not more than two) optimally necessary for national development, which would correspond to the scale of the country and the size of the population.

Latvia has five statistical (NUTS III) regions, of which, the borders do not coincide with the borders of the five planning regions. The planning regions and statistical regions are different and the planning regions are also changing due to the administrative territorial reform. There are five regions in Latvia: the Riga region, the Vidzeme region, the Kurzeme region, the Zemgale region and the Latgale region (Map 1).

Map 1. Statistical regions of Latvia (NUTS III)



The **Riga region** is located in the centre of the country and it is the region driving the development of the whole country. Riga is a typical urbanised region that exists around all capital cities of Europe and other large cities. In 2001, approximately 1 million people or about 40% of the Latvian population resided in the Riga region. The region produces 62% of the national country GDP. Agriculture, near Riga, is more diverse than anywhere else in the country because of market outlets in the city.

The **Vidzeme region** is located in the north-eastern part of the country and it borders Estonia and Russia. Vidzeme is the only region where more than half the inhabitants live in rural areas – 59%, consequently, the region is the smallest according to the density of the population per km^2. According to the economic indicators, Vidzeme and Zemgale, may be characterised as a moderately developed regions of Latvia. The rural tourism sector may offer substantial new employment and income generating opportunities. The advantage of Vidzeme is that the region may offer a wider range of active tourism products both during the winter and summer seasons. The employment structure of the region reflects the results of the economic restructuring process – the number of persons employed in agriculture is decreasing and the number of those employed in industry and the service sector, is increasing. One more feature of employment in the region is the migration to Riga for employment purposes, which deprives the region of its most qualified workers.

The **Kurzeme region** is located in the western part of Latvia and borders Lithuania. The region has the longest coastal area of the Baltic Sea and the Gulf of Riga. Since ancient times the region is famous for its seafaring and fishing traditions. As regards the transport infrastructure of the region, similar to other regions, the biggest part of the National funding is for the maintenance and improvement of roads that connect the biggest development centres (Ventspils and Liepaja) with Riga. The internal and surrounding infrastructures for the ports, as well as access roads, are being developed according to the financial constraints and the requirements of the area. A positive aspect in the development of human resources is the operation of universities in Liepaja and Ventspils that allow flexibility in adjusting the training of students to the demands of the market, such as IT specialists, tourism specialists and managers.

The **Zemgale region** is located in the central part of Latvia, south of Riga, and has a long land border with Lithuania. The most fertile soils are in the Zemgale region. Like other parts of Latvia, the roads to the capital are the only ones maintained in a satisfactory condition in Zemgale. At the same time, the quality of roads connecting district centres and other populated areas in the region is critical. The unemployment rate in the region is high. Many inhabitants of Zemgale have found suitable employment in Riga and they commute to the capital every day, returning to the region in the evening. Zemgale has a rich natural and cultural heritage, which attracts an increasing number of local and foreign tourists. Tourism infrastructure is developing around roads, but the access to road infrastructure and tourism infrastructure is not up to modern requirements. It is related to the limited financial resources available and the lack of knowledge of the requirements.

The **Latgale region** is located in the eastern part of Latvia and has the longest land border with the three neighbouring countries of Latvia – Russia, Belarus and Lithuania. One of the biggest problems of the Latgale region has been the huge levels of unemployment. Although the level of unemployment shows a slight tendency to decrease, it is still the biggest problem in the region, and causes poverty, social alienation, alcoholism, drug addiction, and difficulties in families, where several generations are often subject to social depression and degradation. Several households, particularly in rural areas, subsist on natural farming, old age pensions of elderly family members and child allowances. Further eastward the soil becomes more and more unfertile and the land is covered by stones, still people are capable of producing good yields of crops, grasslands or legumes. The Latgale region is characterised by an ecologically pure environment, high level of biological diversity, picturesque landscapes and many lakes. This provides many possibilities for the development of rural or recreational tourism, which becomes more and more popular among urban inhabitants, in particular, the inhabitants of Riga.

Table 1. Main indicators of regional development in Latvia in 2002

Regions	Number of population in September of 2002		Number of employed population in rural areas		Number of employed population in agriculture, hunting and forestry		Territory		GDP in 2000
	Thsd.	% of total number	Thsd	% of total number	Thsd	% of total number	Thsd km^2	% of total number	LVL million
Riga region	940.4	40.3	42.5	14.0	13.1	8.9	3 450	5.3	2 704.5
Vidzeme region	354.2	15.2	83.2	27.5	38.5	26.2	19 792	30.6	368.6
Kurzeme region	315.6	13.5	51.6	17.1	24.5	16.7	13 601	21.1	586.9
Zemgale region	346.5	14.9	75.6	25.0	43.6	29.7	13 199	20.4	358.5
Latgale region	374.8	16.1	49.6	16.4	27.3	18.6	14 547	22.	323.9
Total in Latvia	2 331.5	100	302.5	100	146.9	100	64 589	100	4 348.3*

* - Excluding extra region – LVL 5.9 million.
Source: Central Statistical Bureau.

Rural development and main problems in rural areas

In order to identify the main problems in rural areas and to discuss rural development policy it is necessary to explain the definition of a rural area as used in this report. The rural area is the whole territory of Latvia, including inland waters and coastal seawaters, excluding such cities as Riga, Daugavpils, Liepaja, Jelgava, Jurmala, Ventspils, Rezekne and Riga district, as well as cities and regional centres. But, it is important to note that in some cases, the statistical information does not correspond exactly with this definition due to the unavailability of some statistical data in the appropriate breakdown. For example, data exists on a district level, but it is too complicated to exclude the centres of districts in order to fit the definition.

About 98% of Latvia is rural, and 32.1 % of the total number of inhabitants reside in rural areas in 2002. The average density of population in the country was 36.6 inhabitants per km^2, in rural areas – 11.65 inhabitants per $km^{2.}$

Structural changes have taken place during the period 1990-2002 in the rural economy, especially in agriculture. The limited employment possibilities in other industries, fall in income, lack of financial capital and economic experience for start up businesses have influenced the migration of the economically more active population from the countryside to towns, especially to the central part of the state – Riga and its region.

Basically all rural areas face the same problems – high unemployment rates, insufficient provision of infrastructure, low entrepreneurial activity, low level of incomes, high proportion of low value added production in the economy and a high demographic burden.

Employment in other industries increases very slowly because the basic industries in the rural economy have comparatively limited alternatives. The actual unemployment rate in the countryside is substantially higher, because several forms of hidden unemployment are more widespread their; for example, the proportion of family members involved in unpaid work is 14% in the countryside, and in towns – 0.3%. The proportion of the employed population in rural areas, which were working part time, was about 15% of total employment in rural areas in 2002. An important problem is the increase in unemployment among the rural population, of pre-pension age (starting from the age of 50 years). The return of the pre-pension age persons to the labour market is made more difficult by psychological characteristics, as most of those people would like to work, but the number of opportunities is limited, and they are not ready or they do not have enough capital to start a commercial operation.

Demographic burden: The demographic burden (number of inhabitants under and above the working age per 1000 working inhabitants) is 793 in rural areas, which considerably exceeds the respective indicator in towns, where the average indicator for the country is 694.

Income of rural population is low. The data on household budgets indicates that the actual income per member of the household has been decreasing every year during the period 1996 to 2000 (decrease from LVL 56.9 to LVL 52.1 in prices of 2000). The average monthly wage and salary in agriculture was about 60% of the average monthly wage and salary of the whole economy in 2002. The results of the population census performed in 2001 indicated that 273.2 thousand or 45.6% of the total rural population were involved, and included self-consumption.

Development of enterprises: There were 42 408 economically active enterprises in Latvia on 1 January 2003. The level of entrepreneurship is low in rural areas. The most economically active enterprises are concentrated in Riga (55% of the total number of economically active enterprises) and in the bigger cities of Latvia (15% of total enterprises). The number of economically active small and medium-size enterprises is similar to the total number of enterprises. Half of them operate in Riga. The distribution of economically active small and medium-size enterprises in Latvia is: micro enterprises – 76%, small enterprises – 20%, medium size enterprises – 4%[1].

Rural structures and infrastructure: At the end of 2001, the total housing stock was 53.5 million m^2, with one-third located in rural areas. In 1990, the housing floor space, average per inhabitant, was 19.9 m^2 (average per rural inhabitant – 23.3 m^2) and in 2001 it was 22.8 m^2 (average per rural inhabitant – 24.8 m^2). Pursuant to the agricultural census data, the floor space of one farm residential building in average was 98 m^2, and 77% of the total number of farms owned at least one residential house. Electricity was not supplied to 2.3% of farms and 23% of farms did not use gas. Almost half of the farms had no telephone, the situation was especially bad in several districts of the Latgale region, where about 60% of the farms had no telephone. Only 0.5% of the farms had an Internet connection.

1. Micro enterprises – less than 10 employees, small enterprises – from 10 to 50 employees, medium size enterprises – from 50 to 250 employees

Objectives of rural and regional development policies

One of the priorities of the Latvian Government is balanced development of Latvia's regions and a high-level of employment. To achieve this, the Government, and the parties comprising it, is committed to the following policies, linked to rural and regional development:

- Improvement of the long-term rural development strategy based on a balanced development of all types and all-size farms in Latvia, provision of new working places, and diversification of the employment profile.

- Concentration of responsibility for matters of regional development and local government affairs in one institution of public administration.

- Provision of mutually co-ordinated work of the Government and regions for planning sustainable development and implementation of these plans.

- Elaborating and implementing the regional policy of the Government, provision of co-ordination of the national economy branches' development and conformity with priorities of regional development.

- In the National Development Plan of Latvia, reflection and substantiation of the possibilities for national development, as well as the development of all regions.

- Elaboration of the National Planning of Latvia including, the national interests and requirements for utilisation of territory, planning and development.

- Reorganisation of the Programme of Regions Requiring Special Support, envisaging direct participation of the regions in decision-making on project approval and the granting of funds.

- Reorganisation of the State Investment Programme, envisaging concrete criteria that would ensure equal opportunities for the realisation of products in all regions.

At the same time, the Law on Agriculture also sets out objectives for rural development. One of the tasks of this Law is to create the preconditions for:

- Development of rational and diverse rural undertakings in order to produce, as far as possible, cheap, qualitative and competitive products, and to increase the effectiveness of agricultural production, ensuring employment in rural areas.

Rural development objectives are fixed in several programmes, for example, in the SAPARD and in the new programme draft for rural development.

Instruments and effectiveness of regional and rural development policies

There are several instruments for the development of entrepreneurship and for providing conditions to increase employment and income in rural areas, but these instruments are mainly financial support and agricultural programmes.

State subsidy programmes

For the enhancement of agricultural competitiveness, the state is providing support in the form of subsidies. Pursuant to Section 16 of the Agricultural Law, subsidies may not be less than three per cent of total expenditure of the annual budget of the state, to be funded out of subsidies from general revenues. Subsidies, like the overall agricultural policy, aim to develop the agriculture sector so that it can be integrated into the European single market and produce products meeting the requirements of international markets, competing with the products of other countries in terms of quality and production costs. The following directions for state support are set out to achieve that goal:

- Technological modernisation of production.
- Quality management through the entire production and sales process.
- Promotion and development of produce marketing.

There are several support programmes: Support for Liming and Melioration, Support for Plant Growing, Support for Cattle Breeding, Credit Guaranty Fund, Support for Technical Modernisation, Support for enhancing the Competitiveness of Dairy Produce, Support for Fisheries and others. The subsidies give additional income and investments for agricultural producers, in order to develop qualitative and competitive products and increase the effectiveness of agricultural production.

Agricultural Long-term Investment Credit Programme

The development of agricultural holdings will be accelerated by the Agricultural Long-term Investment Credit Programme adopted by the government in 2001 and started in the Spring of 2002. This programme is mainly aimed at providing long-term finance for agricultural holdings, expediting the attraction of investment for creation of farms of optimum size and enhancing the competitiveness of agricultural holdings. The programme also strives to make cheap loan facilities available to Latvian farmers. This form of credit was particularly fostered by the implementation of the subsidy programmes and SAPARD for the development and technological modernisation of agricultural production, which gave rise to greater demand for loans by farmers.

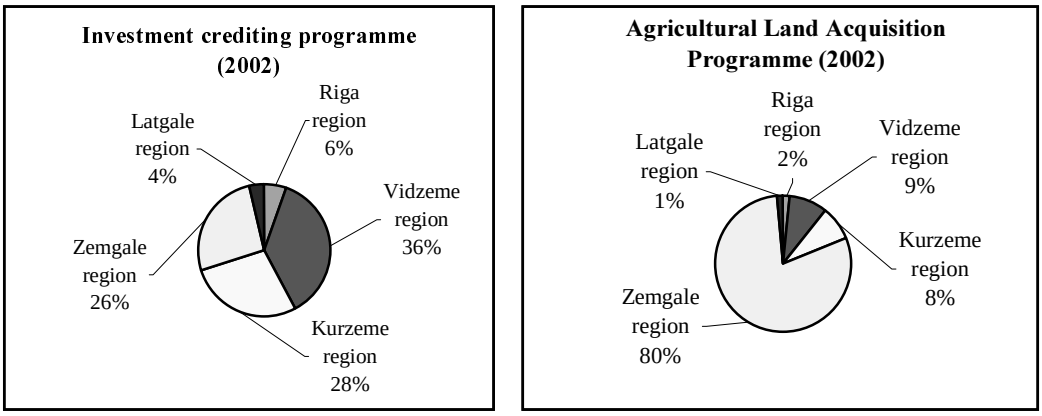
In 2002, the total amount of loans that were granted was estimated at 1.98 million lats. The highest amount was granted to farmers in the Vidzeme region (about 36% of the total – see Figure 1), mainly for development of the dairy sector. The next sector, to which a lot of loans were allocated, was crop production and modernisation and these loans were used by farmers in the Kurzeme and Zemgale regions.

Agricultural Land Acquisition Credit Programme

In July 2002, the Agricultural Land Acquisition Credit Programme started to operate. The programme is aimed at launching the mechanisms for the efficient functioning of the agricultural land market by supporting the development of competitive production areas, meeting the European Union standards, and the consolidation of lands in order to encourage the efficient cultivation of agricultural land. This programme is mainly for the granting of long-term (15-25 years) loans for the acquisition of agricultural land. It is possible to receive loans under this programme with an interest rate of 4%. One of the additional effects of this programme could be that unused agricultural area would decrease, and landscapes in rural areas could be improved.

In the framework of this programme, most of the loans were used in the Zemgale region (about 80% of the total), which were taken for cereal and sugar beat production, which are typical agricultural activities in this region. Less active farmers were found in the Latgale region, which used only 1% of the loans granted in 2002.

Figure 1. Distribution of granted loans for investment credit and land acquisition in regions of Latvia in 2002, %



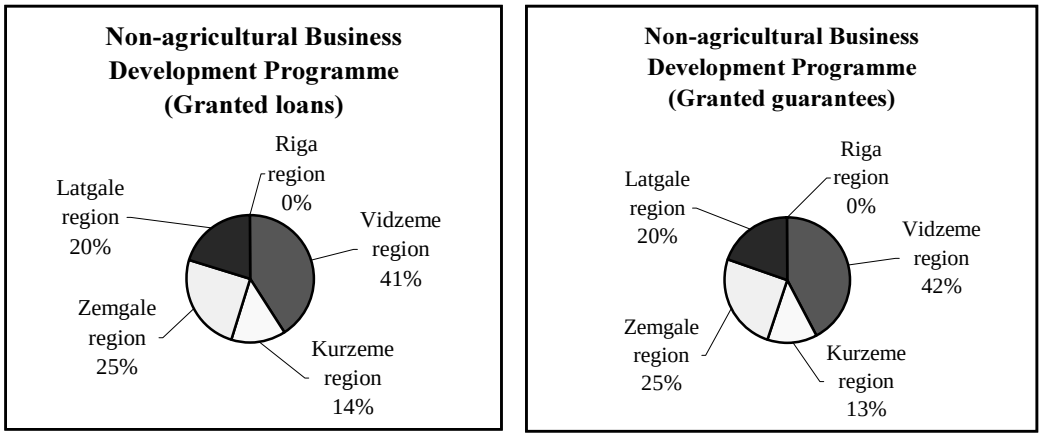
Source: State Owned Joint Stock Company Mortgage and Land Bank of Latvia.

Non-agricultural Business Development Programme

At the end of 2002, the government adopted the Non-agricultural Business Development Programme and it has been in operation since 2003. The overall aim of the programme is to facilitate the economic development in rural areas by supporting non-agricultural businesses, improving infrastructure, improving the rural landscape to meet the business requirements and observing environmental protection requirements. The State Owned Joint Stock Company Mortgage and Land Bank of Latvia are involved in the implementation of the programme by granting loans. The Rural Development Fund by granting guarantees for the businesses, in case of insufficient loan guarantees, the Rural Support Service for giving grants, and the specialists of regional development agencies for local initiatives, training of people and the attraction of businesses. The total amount of funding for the programme is LVL 5.2 million.

As shown in Figure 2, the most active region is the Vidzeme region, where most of the loans and guarantees are granted for non-agricultural businesses. The Riga region is not eligible to get such loans and therefore, the share of granted loans and guarantees is zero. About 43% of the loans and 47% of the guarantees were used for tourism development. The second largest sector was wood processing and this sector used about 17.5% of the loans.

Figure 2. Distribution of granted loans and guarantees in different regions, at the end of 1st quarter of 2003, %



Source: State Owned Joint Stock Company Mortgage and Land Bank of Latvia.

Loan guaranties for rural businesses

The state-stock Company Rural Development Fund has been established to issue guarantees for businesses – borrowers – in the event of insufficient loan security. A total of 466 loan guarantees for LVL 4.83 million has been granted since 1997, when the RDF commenced guaranteeing the loans. Based on those guarantees, rural businesses have received loans amounting to LVL 16.1 million. Starting from 2002, the Rural Development Fund is also guaranteeing the loans taken within the SAPARD programme and the Agricultural Long-term Investment Credit Programme.

Foreign financial support for rural, agricultural and forestry development SAPARD

On 6 December 2001, the Commissioner Mr. F. Fischler approved the decision (2001/885/EC) providing aid for implementing agencies for pre-accession measures in agriculture and rural development in the Republic of Latvia in the pre-accession period. The decision was published in the Official Journal of the EU on 12 December 2001 (L327/45), and it means that the accreditation of the Rural Support Service (RSS) was recognised by the European Commission.

There are several objectives attributed to each measure within the SAPARD Rural Development Plan. A submission of projects, with a view to receive aid under the Programme, started at the end of December 2001, but rural entrepreneurs received the first refunds from SAPARD, only from 15 April 2002

Table 2. The main priorities and measures of SAPARD in Latvia

Priority	Priority Measures
Priority 1. Investments in Agricultural Holdings	Measure 1.1. Modernisation of Agricultural Machinery, Equipment and Construction of Buildings Measure 1.2. Afforestation of Agricultural Land Measure 1.3. Land Reparcelling (planned measure)
Priority 2. Improvement of Agricultural and Fisheries Product Processing and Marketing	Measure 2.1. Improvement of Agricultural and Fisheries Product Processing and Marketing
Priority 3. Development and Diversification of Economic Activities Providing Alternative Income	Measure 3.1. Development and Diversification of Economic Activities Providing Alternative Income
Priority 4. Improvement of Overall Rural Infrastructure:	Measure 4.1. Improvement of Overall Rural Infrastructure
Priority 5. Environmentally Friendly Agricultural Methods	Measure 5.1. Organic Farming (planned measure) Measure 5.2. Preservation of Biodiversity and Rural Landscape (planned measure) Measure 5.3. Reduction of Agricultural Runoff (planned measure)

The bulk of projects implemented under SAPARD measure 1.1. “Modernization of agricultural machinery, equipment and construction of buildings” falls within the grain sector: 79 projects or 65.4% of the total number of implemented projects, and in the milk sector – 43 projects or 30.7% of all the projects under the measure. In the pig sector 5% of projects were implemented, in the fruits sector – 4.3%, in the vegetable sector – 2.1%, but in the poultry sector and in establishing tree nurseries - only 0.7% of the total number of projects were implemented.

Under measure 1.2. “Afforestation of agricultural land”, 31 project or 25% of the supported projects have been implemented, on average, the sum requested by one applicant is LVL 4 608, being the least as compared with other measures.

Under measure 2.1. “Improvement of agricultural and fishery product processing and marketing”, only one project has been implemented in the fish processing sector, with the sum claimed equal to LVL 59 227.

Under measure 3.1. “Development and diversification of economic activities, providing alternative income”, the bulk of projects has been implemented in the area of technical services – 9 or 40.9% of the total number of implemented projects. In rural tourism – 7 projects (31.8%) have been implemented, in non-traditional agriculture – 4 projects (18.2%) and in craftsmanship – 2 projects (9.1%). The highest requested sum falls within craftsmanship – LVL 49 380, but in non-traditional agriculture, on average, 3 times less – LVL 16 100.

Under measure 4.1. “Improvement of general rural infrastructure”, 1 project has been implemented (33.3% of the total number of projects under this measure) in association with the installation of a water supply system with the sum of eligible costs LVL 4 813, but 2 projects (66.6%) were focused on upgrading of the rural establishments and farm access roads, requesting, on average, LVL 30 883. In other sectors, no projects have been implemented.

Small and medium-size enterprise credit programme

This programme started at the beginning of 2000. It is aimed at financing small and medium-size enterprises thus promoting the creation of new workplaces, and financing of projects by beginners in business and projects without sufficient security. The State Owned Joint Stock Company Mortgage and the Land Bank of Latvia were involved in the implementation of the programme in order to grant loans to enterprises on special conditions.

Programme on Specially Supportable Regions

The Programme on Specially Supportable Regions has been in operation since 1997 in accordance with the Law on Specially Supportable Regions. Specially Supportable Regions are defined as the territory where a negative economic impact and social development trends have been lasting for a longer period or which have been granted a special status by the Government. Such a status is revised every three years. This status was first granted in 1997 to 84 territories of municipalities.

In 2001, the special status was given to 135 territories of municipalities. The Regional Development Law adopted by Saeima provided, that The Law on the Specially Supportable Regions should be abolished. In accordance with the transition rules of the Regional Development Law, the status of the specially supportable region is in force until 27 June 2004 and the Regional Fund continues its promotion of enterprise development in accordance with the special Government rules. The Regional Development Law maintains the idea of specially supportable territories and promotes the development of socially and economically least developed territories to achieve equivalent development potential in the country. The Regional Development Law provides, that the Bureau of Region Development Planning will grant and abolish the status of specially supportable regions in the future and the finances will be allocated for regional development in accordance with procedures provided by the government. In accordance with the Regional Development Law, the Ministry of Regional Development and Local Governments of Latvia will draft the Government rules "The procedure for granting and abolition of the specially supportable regions" by 1 June 2003.

After June 2004, support for the specially supportable regions will be granted from resources of the Regional Fund. In the future, the control of the Regional Fund resources will be in the non-income state limited organization Regions Development competition, which is planned to be transformed into the State Regional Development Agency.

In the period from 1998 until the end of 2002, LVL 4.5 million was spent from the Regional Fund resources. About 95% of the total resources was invested in the specially supportable regions, of which, 0.54% is co-financing of PHARE projects, 4% for educational and information activities and 90.7% is direct support to entrepreneurs and local-government projects in the specially supportable regions. The other expenditures of the Regional Fund are 4.76%.

State Investment Programme

To consolidate the expenditures of the budget resources for capital investments, as well as to increase their effectiveness, the State Investment Programme is being developed in Latvia (since 1995), but it does not cover all the State investments – only half of them. The rest of the State investments are funded from special budgetary funds and self-government budgets.

In the regional profile, the State investments can be associated with a region or cover the whole territory of Latvia. In the period from 1999 to 2001, regions were granted LVL 393.6 million. At that

time, the bulk of these resources were granted to the Riga region and the least to the Vidzeme region. But in the period from 1999 to 2001, 43.4% of all investment resources were invested without any specific regional distribution.

Analysing investment objectives by regions, it becomes clear that part of the investments in all regions was channelled to environmental protection. In the Kurzeme region, the major part of investments annually, on average, was allocated to the development of the transport sector (77%); in the Zemgale region to environmental protection (50%); in the Vidzeme region – to environmental protection (53%); in the Latgale region to environmental protection (68%); and, in the Riga region the highest share of investments goes to environmental protection (36%) and to power supply (36%).

National Development Plan

The Cabinet of Ministers approved the National Development Plan in December 2001, which is one of the key strategic planning documents designed for the period 2003-2006. It is harmonised with the Long Term Economic Development Strategy of Latvia and reflects the priorities, tasks and consistency of their implementation defined in the strategy with the aim to foster socio-economic development in Latvia. The main objectives of the National Development Plan are to promote:

- Sustainable development of Latvia by improving welfare and social protection for every person.
- Regional development by decreasing and eliminating the unfavourable regional differences and supporting a favourable regional disparity.

The documents also set the following priorities:

- Promote the development of the economy and competitiveness.
- Develop human resources and promotion of employment.
- Sustainable and balanced development of the whole territory of the state.

After the accession of Latvia to the European Union, this plan will be transformed into a Single Programme Document, which will draft financial support to development projects from EU Structural Funds, retaining at the same time, the impact on distribution of local public investments and attraction of alternative financing. To attract resources of various EU funds for the development of priorities identified in the National Development Plan of Latvia immediately after the accession, work on another strategic document – the Development Plan (Draft Single Programming Document) – was started in 2002.

Involved institutions in rural and development policies

There are several institutions and ministries involved in rural and regional development. For example, the Ministry of Agriculture is responsible for state policy in the spheres of food safety, agriculture, forestry, fishery, preservation of natural resources and rural development.

The Ministry of Economics, for example, is responsible for the development and implementation of the State's national policy for economic development.

One useful addition came with the establishment of a new Ministry - the Ministry of Regional Development and Local Governments in Latvia, which started to operate officially at the beginning of 2003.

All of these Ministries are responsible for certain sectors, but at the same time co-operation should be improved to ensure a well co-ordinated policy of rural and regional development. Currently, the Ministries are responsible for the programmes but these are not linked, and the efficiency of these programmes is not evaluated.

The future policy measures and instruments

Development Plan

The Development Plan (Draft Single Programming Document) and other documents attached to it will become the basis for the allocation of resources from the EU structural funds and the Cohesion Fund in Latvia. The objectives of this document are the following:

- Promoting Competitiveness and Employment.
- Development of Human Resources.
- Development of Infrastructure.

Table 3. Priorities, measures and planned finance of the Single Programming Documents

Priority	Priority Measures
Promotion of Territorial Cohesion (29.2% of all finance of Structural Funds – 161.74 MEUR)	• Capacity Building for Regional Development (2% of the total priority financing are allocated to this measure). • Improvement of Quality of Environment and Infrastructure (29%). • Development of accessibility and transport system (44%). • Development of information and communication technologies (10%). • Development of healthcare and education infrastructure (15%).
Promotion of Enterprise and Innovations (29.2% of all finance of Structural Funds – 161.77 MEUR)	• Measures for applied R&D in enterprises, innovation and technology transfer (15% of the total priority financing are allocated to this measure). • Development of business related infrastructure (45%). • Support for increasing the competitiveness of enterprises (15%). • Accessibility to finance for business (25%).
Development of Human Resources and Promotion of Employment (20.4% of all finance of Structural Funds – 113.23 MEUR)	• Promotion of employment (43% of the total priority financing are allocated to this measure). • Development of education and continuing training (38%). • Combating social exclusion (19%).
Promotion of Development of Agriculture and Rural Areas (14.6% of all finance of Structural Funds – 80.89 MEUR)	• Investments in agricultural holdings (25% of the total priority financing are allocated to this measure). • Young farmer support (5%). • Improvement of processing and marketing (21%). • Land improvement (5%). • Preservation of rural landscape (5%). • Diversification of rural economic activities (25%). • Development of sustainable forestry (5%). • Development of local capacities supporting sustainable rural communities (LEADER+ type measure) (2.5%). • Training (2%). • Consultations (2%). • Afforestation of abandoned agricultural land (2.5%).
Promotion of Sustainable Fisheries Development (3.9% of all finance of Structural Funds 21.58 MEUR)	• Adjustment of fishing effort (30.5% of the total priority financing are allocated to this measure). • Fleet renewal and modernisation of fishing vessels (15.3%). • Improvement of processing and marketing of fishery and aquaculture products (15.6%). • Development of aquaculture (3.1%). • Fishing port facilities (18.7%). • Small-scale coastal fisheries (9.7%). • Socio-economic measures (3.4%). • Acquisition and promotion of new market outlets (1.8%). • Support to members of trade and producer organisations (1.9%).
Technical Assistance (2.7% of all finance of Structural Funds - 15 MEUR)	

Source: Draft Single Programming Document 2004–2006.

Draft for the Rural Development Plan of Latvia

The Rural Development Plan defines the priorities for the 2004-2006 programming period, and the rural development measures chosen for the attainment thereof, in accordance with the EC Regulation 1257/99 are those, which are important and able to supplement the instruments already used for the national development policy by providing a substantial long-term contribution to the attainment of the strategic objectives of the rural development.

The Government is setting forth the following priorities in the implementation of the plan:

- Priority 1 - Development of an Efficient, Flexible and Sustainable Rural Economy.
- Priority 2 - Preservation of a Biologically Diverse Rural Environment.

The implementation of the objectives shall promote the existence of alternative economic activities, increase rural employment and opportunities to increase the income and welfare level in rural economy, in addition to producing modern and competitive produce within the agricultural sector. It will also promote resource-saving and the renewal of forestries. The main measures and objectives of the Draft of the Rural Development Plan, which will be financed from the EAGGF Guarantee Section, are the following:

Table 4. Measures and targets of the Draft Rural Development Plan of Latvia

Measure	Target
Agro-environment	To implement and to promote the methods of farming, which are friendly to the environment, which preserve rural landscapes and to promote the production of quality organic products and reduce environmental pollution.
Less-favoured areas and areas with environmental restrictions	To facilitate economic activities, employment, income and welfare for inhabitants in the area, in which there are limited possibilities to increase the income of rural households due to less favourable climatic conditions.
Early retirement	To promote the involvement of young people in the rural economy and to provide incomes for older farmers.
Afforestation of agricultural lands	To facilitate the use of less fertile and unutilised agricultural lands, and to promote the improvement of rural landscapes.
Support for producer groups	To facilitate the formation of producer groups to provide effective agricultural production, primary processing and marketing, lowering costs of production.
Support for semi-subsistence agricultural holdings	To speed up structural changes in the rural economy, to facilitate the development of activities in the non-agricultural sector, and to increase employment in rural areas.

Source: Rural Development Plan of Latvia.

Conclusions

Finally, summarising the conclusions on the situation and implementation of policies for rural and regional development, it is necessary to highlight the following:

- Significant structural change has taken place during the period of 1990 to 2002 in the rural economy, especially in agriculture. There are limited employment possibilities in other industries. The fall in incomes, lack of financial capital and economic experience for starting

up new activities have influenced the migration of the economically more active population from the countryside to towns, especially to the central part of the state –Riga and its region.

- The problems are similar in all rural areas are similar – a high unemployment rate, insufficient provision of qualitative infrastructure, low entrepreneurial activity, low level of incomes, high proportion of low value added production in the economy, and a high demographic burden.

- The proportion of the employed population in rural areas, which were working part time, was about 15% of the total employment in rural areas in 2002. An important problem is the rise in unemployment among the rural population of pre-pension age, starting at the age of 50.

- The level of entrepreneurship is low in rural areas. The most economically active enterprises are concentrated in Riga and in the bigger cities of Latvia.

- One of the priorities of the Latvian Government is: a balanced development of Latvia's regions, a high-level of employment, as well as improvements in the long-term rural development strategy, based on balanced development of all types and all-size farms in Latvia, the provision of new work places, and diversification of the employment profile.

- There are several instruments for the development of entrepreneurship and the provision of conditions for increased employment and incomes in rural areas, but these instruments are mainly financial support and programmes of agriculture, such as the State Subsidy Programmes, Agricultural Long-term Investment Crediting Programme, Agricultural Land Acquisition Crediting Programme, Non-agricultural Business Development Programme, Foreign Financial Support for Rural, Agricultural and Forestry Development SAPARD.

- For regional development, there are other programmes: the Programme of Specially Supportable Regions, which is in operation since 1997 in accordance to the Law on Specially Supportable Regions. In the period from 1998 to 2002, LVL 4.5 million was spent from the Regional Fund resources. About 95% of the total resources were invested in the specially supportable regions.

- In the regional profile, the State investments can be associated with a concrete region or cover the whole territory of Latvia. In the period from 1999 to 2001, regions were granted LVL 393.6 million. At that time the bulk of these resources was granted to the Riga region, and the least to the Vidzeme region. But, in the period from 1999 to 2001, 43.4% of all investment resources was invested without any specific regional distribution.

- Several Ministries are responsible for certain sectors, but, at the same time co-operation should be improved to ensure a well co-ordinated policy of rural and regional development. Currently, the Ministries are responsible for programmes, but these are not linked, and the efficiency of these programmes is not evaluated.

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LITHUANIAN RURAL AND REGIONAL DEVELOPMENT

Part I

By Dr. Donatas Stanikūnas, Dr. Raimundas Dužinskas and Ms. Erika Ribašauskienė
(Paper presented by Dr. D. Stanikūnas)

Abstract

This report deals with the situation in rural areas in Lithuania. The main problems of rural development are identified: the low income of rural population, big and growing unemployment, regional income differences. The main activity for the Lithuanian rural population remains agriculture. About 50% of the Lithuanian rural population are engaged in agriculture. The concentration of many rural dwellers in agriculture and the low incomes arising from it determine the importance of diversification, and the necessity to reform agriculture. The reduction in the number employed in agriculture is considered as a positive change, which is determined by the reform and modernization in agriculture. The slow development of small and intermediate businesses does not compensate for the increase need for new jobs in rural areas. The natural, economic and social factors of rural development in various rural areas of Lithuania differ significantly. Rural and regional development is necessary in order to identify rural regions, and to determine the main problems and priorities.

Rural development in Lithuania

Rural regions of Lithuania comprise villages of different types, towns and associated land, their inhabitants with their living environment, its conditions and quality, lifestyle based on regional culture, and suitable economic activities. Rural areas cover 97% of the state. One-third of Lithuania's population live in villages. More than half of Lithuania's rural areas are suited for agriculture. The country's population has preserved the major part of the nation's cultural and historical heritage. The country's lifestyle and traditions represent the national culture. Lithuania's rural areas have a big potential for recreation business.

Due to the East and Central European countries' integration into the EU, the cohesion of participating states' and regions' development processes are taking place. The same is true for understanding the solutions of how the economic, environmental, cultural and social problems should be solved. A vision of an integral rural development predominates in the EU agricultural and rural development policy that preconditions qualitative and quantitative changes, in which, the rural population, communities and institutions participate in creating better living standards, an acceptable environment and providing better opportunities for personal development. The principles of the EU rural strategy were set during the European Conference that took place in Cork, Ireland (in November 1996). The main principles are the following:

- The priorities of rural development should be set, taking into consideration specific regional resources, social and demographic situations and possibilities for economic activities.

- The principle of integration: rural problems are versatile. They include not only the agricultural sector, but also the social and environmental spheres and business development.

An integrated approach towards the countryside and integrated support system should be taken to solve these problems.

- The principle of variety: the established priorities of rural development should be integrated into the diversification of economic, social and cultural activities.

- The principle of continuity: the policy of rural development should preserve natural resources, variety of plants and regional cultural identity for future generations.

- The principle of self-governance (local independence): rural development should be decentralised, as much as possible, striving to mobilise the creativity and solidarity of rural communities.

- Financing: local funds should be used as the main financing source for rural development; assigning private and state funds to support small and medium-size enterprises and to diversify other rural businesses and cultural activities.

- Administration: the potential and effectiveness of state institutions are consolidated on the regional and national levels raising qualifications, improving communication measures and machinery, sharing experience, and creating a common system of European regions and communities.

Usually, to implement these principal regulations, plans or programmes of rural development are prepared.

The rural development trend becomes one of the most important concerns in Lithuania's agriculture policy, and becomes one of the most important agricultural policy divisions. The proportion of support for agriculture and for rural development has changed substantially. Regional development is brought into focus. During the period 1997–2002 strategies, programmes, rules of law, that helped to change the public opinion on how the rural and regional problems should be solved, were elaborated. The "National Strategy for Agricultural and Rural Development 2000–2006", contains programmes on implementation measures "Strategy for Agricultural and Regional Development 2000–2006", that covers the "Long Term Lithuanian Economy Development Strategy for the period by the year 2015" which in turn includes the "Rural, Agricultural and Fishery Development Strategy for the period by the year 2015".

After the accession into the EU, Lithuania's rural development policy will be incorporated into the EU rural development policy. That is the reason why at present, Lithuania's rural policy is being harmonised with the EU rural policies. The Agriculture and Rural Development Law came into force on 1 January 2003 and it provides the major EU legislation for Lithuania's rural development policy. This presumes that rural development will improve the rural population life standards, maintenance of village economic and social structures, improving community member interaction in order to secure economic and social harmony protection and maintenance of ethnic culture, landscape and environment. Lithuania's rural and regional problems include growing unemployment, low agriculture production productivity, and the need for alternative income sources in rural areas. The whole administration system should focus on diminishing regional income differences of the rural population, human resource training, sustainable development of country districts, cultural and mental progress of the country's communities.

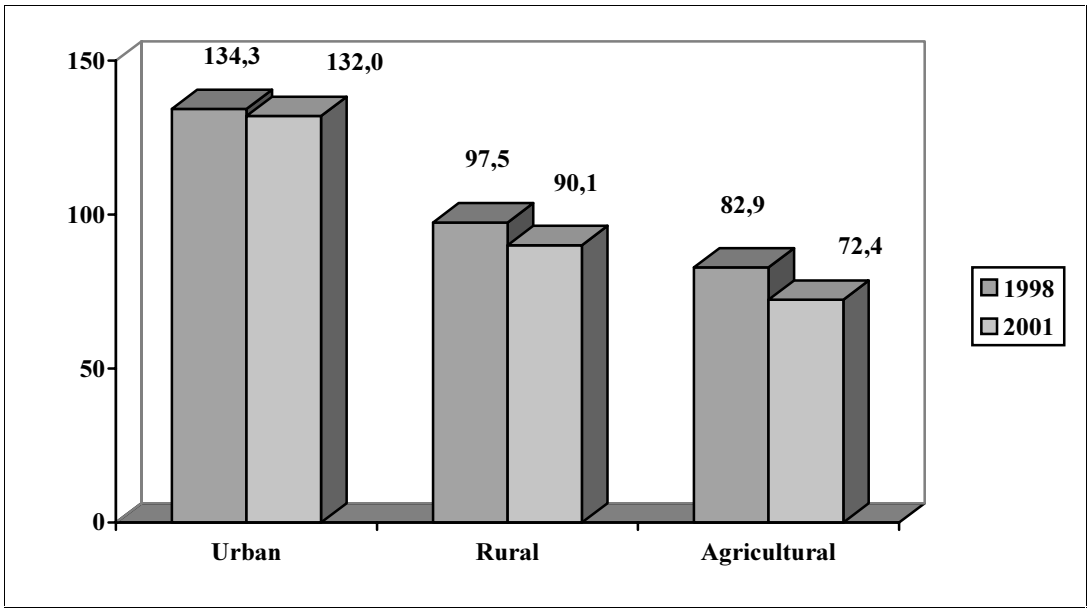
Problems in rural areas

The most vital aspects of rural development in Lithuania are problems that threaten the rural population: low income, big and growing unemployment, and regional income differences.

Income disparities between the rural and urban population are growing. Compared to urban household member income per capita, rural household member income is smaller by 33%, and agriculture's by 50%. During 1998-2002, the urban resident income increased by 3% a year, while rural resident income increased by 1% a year, and agriculture workers' income decreased by 1%.

Rural household members income constituted only a portion of the urban one: 72.6% in 1998; 68.2% in 2001, and agricultural workers' 61.7% and 54.9% respectively (Figure 1). A substantial and growing part of the available income constitutes income not related to occupation – social subsidies, pensions, etc.

Figure 1. Household members average available income in 1998-2001 in EUR per head



Source: Household Income and Expenditure 1998, 2001, Department of Statistics, Government of the Lithuanian Republic.

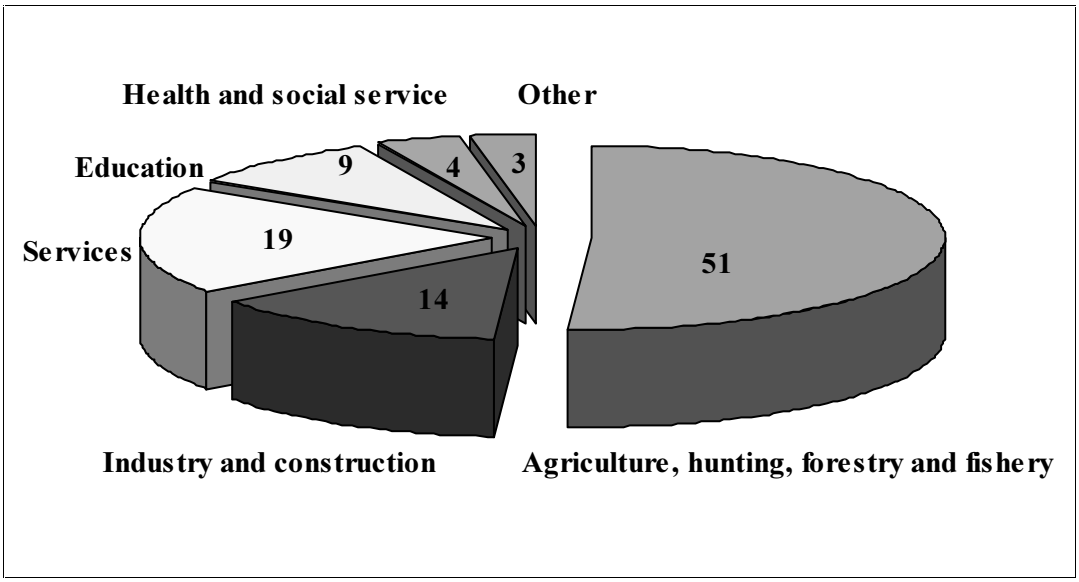
Among the village population, a high level of poverty 27.3% continues to exist. Different categories of the rural population are exposed to poverty, to a different extent. In recent years, people employed in agriculture became most threatened by poverty.

Agriculture remains the main occupation of the village population. One half of Lithuania's rural inhabitants receive income from agriculture (Figure 2). During 1998-2001, other economic activities became just a bit more important: services by 2%, education by 1%, while other activities remained the same.

Institute questionnaires on rural diversification of economic occupations returned data showing that 20% of the people engaged in agriculture also engage in side activities: agriculture product processing and salesmanship, country tourism, crafts, other services and jobs. Side activities usually

have farmers cultivating up to 10 ha. Agriculture workers and small farm owners that, do not have side activities, usually have a subsistent lifestyle.

Figure 2. Economic activities of rural population in 2001, %



Source: Workforce, Employment and Unemployment in 1998-2001, Vilnius, Department of Statistics, Government of the Lithuanian Republic, 2002.

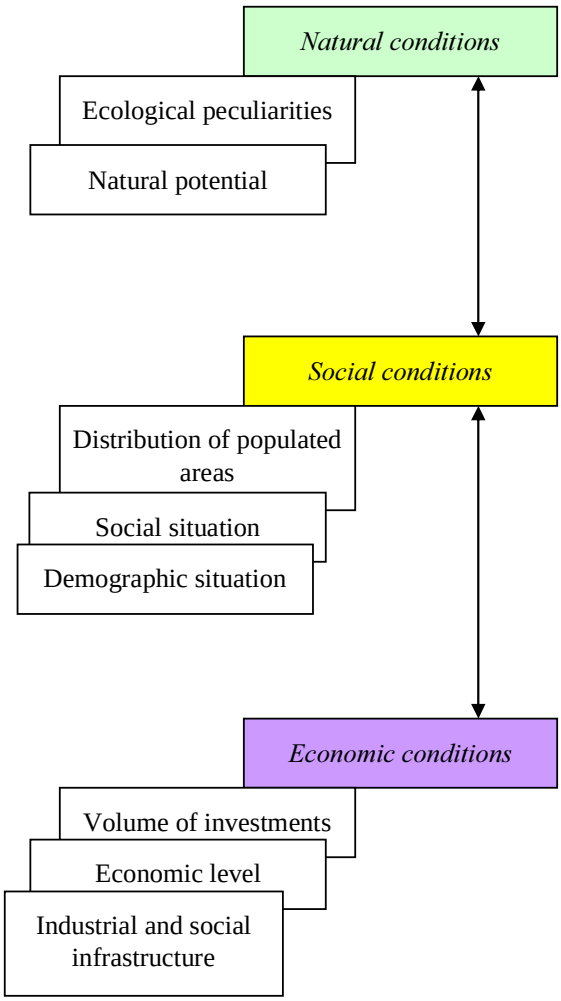
Bearing in mind the recent challenges for the rural population that concentrates on agriculture production that provides low income, a solution is supposed to come from rural economic activities; diversification and agriculture restructuring, Agriculture related employment reduction, facilitated by agriculture restructuring and modernisation, seems to be a positive trend. Unfortunately, the slow development of small and medium businesses provides little employment opportunities, and do not solve the rural unemployment problem. In 2001, there were 14.4% of jobless people in rural areas. During the last 4 years the unemployment level rose more rapidly than the number of newly employed persons. More than one-third of the unemployed used to work in agriculture. The biggest fractions of jobless rural inhabitants are in the 20–29 age group, that is 36%, and in the 35–39 group, that is 11%. Young people with insufficient professional training are condemned to unemployment. Agriculture absorbs those unemployed into small, usually family farms, but it is not a competitive occupation and does not provide sufficient income for families.

Regional development

The research carried out on the situation of rural areas shows that regional demographic, economic and social differences are significant. Therefore, regional policy should be implemented taking into consideration the advantages of Lithuania's nature and regional peculiarities, which have formed and continue to form different economic, cultural, social and demographic situations and conditions to develop various activities.

To design rational and useful programmes of regional development and to achieve the main objective of the state regional policy, the identified regions should be integrated, as much as possible, according to the main characteristics, which influence territorial differentiation of the state's social, economic and ecological policy (Figure 3).

Figure 3. Conditions and factors that influence the development of rural areas

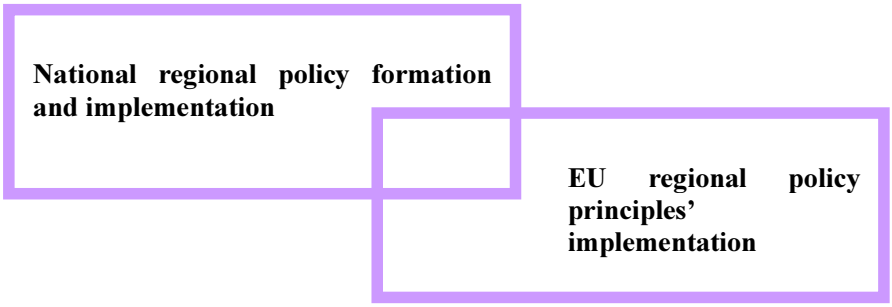


Regional policy in Lithuania begun in 1998, when the Government passed the bill "Outlines of Lithuanian regional policy". The "Regional Development Act" serves as a foundation for regional policy. The "Preparation for EU Membership Programme" and the "Middle Term Economic Development Strategy" also supported the basic trends.

Facilitation of regional economy reorganization and modernization, accelerating the cohesive development of different regions, the reduction of regional, social, and economic differences, the reduction of unemployment are all basic objectives addressed by the "Regional Development Act".

Regional policy in Lithuania is composed of two constituents: the national regional policy component with implementation measures (the main aim is a reduction of regional development differences), and the EU regional policy principles' implementation (after accession Lithuania will be considered as a single region with corresponding needs for structural support) (Figure 4).

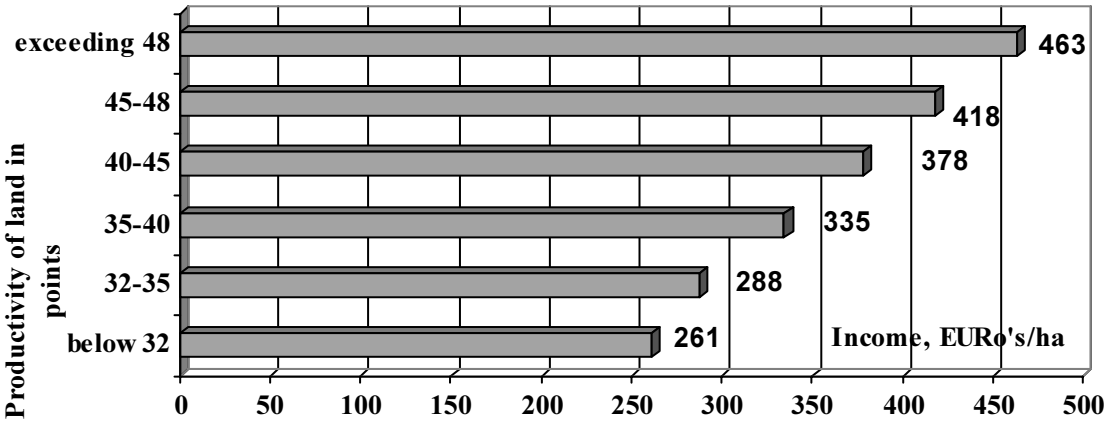
Figure 4. Lithuanian regional policy structural elements



At present, Lithuania's regional policy consists of two elements: the local regional policy (vertical) element, and the co-ordinating local policy (horizontal) element. The vertical element comprises measures designed to solve specific local regional problems, and the horizontal element consists of different economic programmes that bear a regional view.

A need for alternative income sources in rural areas varies remarkably in the different regions of Lithuania. According to the environmental conditions, the prevailing economic activities vary widely, *e.g.* Gross Domestic Product created in agriculture ranges from 23% to 83%. The Lithuanian rural and regional demographic situation depends on life standards. The population density depends on the productivity of land, which varies from 8.6 to 40.2 head per square kilometre, and the proportion of births to deaths varies from 0.37 to 1.36 (Figure 5).

Figure 5. Regional income differences in agriculture



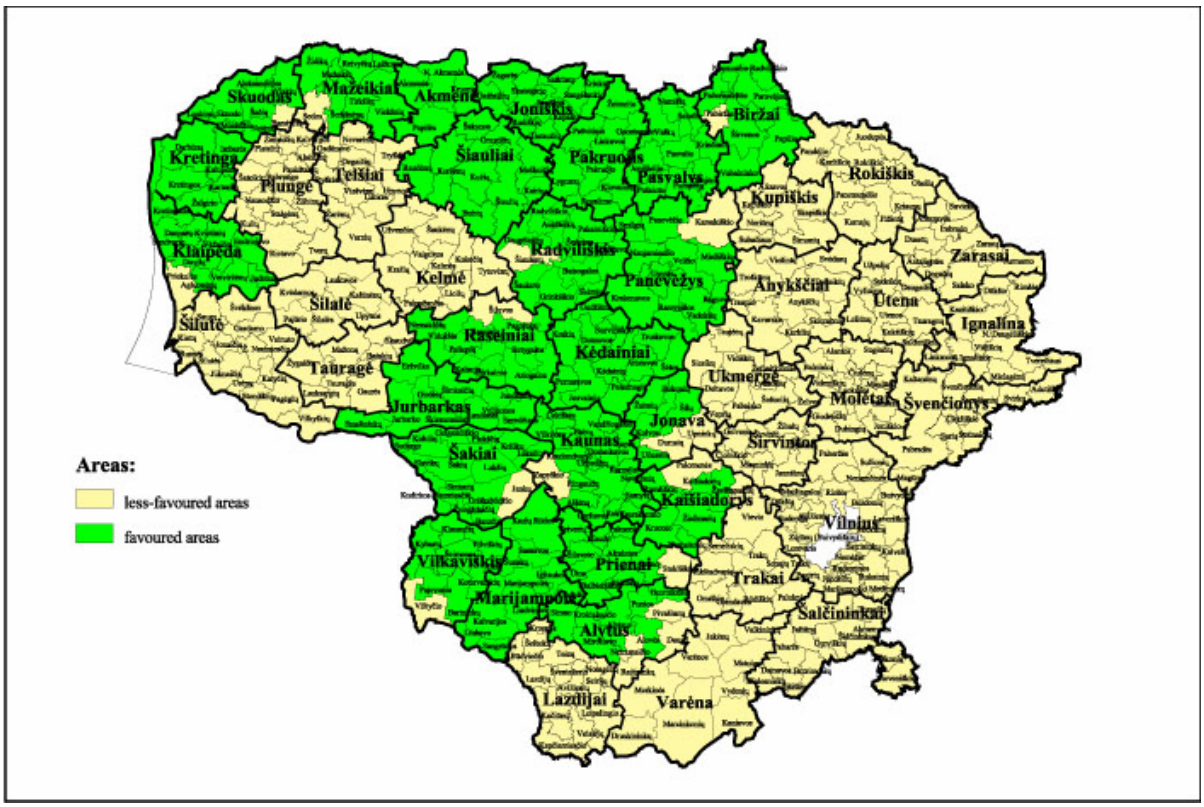
Source: Lithuanian Institute of Agrarian Economics Scientific Research.

Lithuania started to implement the agriculture income support system that suits EU requirements in order to reduce regional differences in living standards in areas less-favoured for agriculture. In 2002, the Minister of Agriculture confirmed the recognition of less-favoured areas criteria on environmental, demographic, economic and development objectives (land quality; agricultural land,

which land quality point is under 32 (in %); density, population per 1 km^2; vitality index; inhabitants over 60 (in %); value created in the agricultural sector over 1 year (in Litas per 1 ha).

Less-favoured areas cover 1 612.2 thousand hectares or 48% of state agricultural land (Map 1).

Map 1. Less-favoured areas in Lithuania



Green colour represents areas with less-favoured soil to farm and other environmental conditions.

In 2002, farmers cultivating less-favoured land received compensatory payments from the "Special Rural Support Programme" pursuant to the European Council regulation 1257/1999/EEC. Agriculture businesses that declared cultivated land area (except desolate, unusable land (unbroken soil) area) received compensatory payments. It should be mentioned that in less-favoured areas sheep breeding is promoted.

The population is older in the less-favoured areas. They find it more difficult to adapt for work under the conditions of the market economy. A larger share of agricultural land is suitable for farming. Therefore, most investments in these areas should be used to develop alternative businesses. In these areas, it is recommended to develop more alternative businesses, non-traditional agricultural activities, fisheries, forestry, rural tourism and recreational services, and small-scale agricultural processing industries.

The EU coherent rural development concept emphasizes the aim to balance agriculture and other rural occupations rationally, using rural resources that would provide for social development in villages. In order to implement Lithuania's rural development instruments effectively and to improve the quality of rural life, it is proposed:

- To stimulate programmes, which would harmonize regional economic and social development, while facilitating rural employment, creativity and realisation.
- To subsidize consulting services, activating local society and improving their entrepreneurial skills, facilitating rural alternative employment.
- To stimulate exhibitions, and seminar organization, which would deal with consulting alternative agriculture production and alternative rural activities employed, focusing on vital technology, economic and judicial topics.
- To stimulate education and the realization of various pilot projects.
- Direct foreign investment in countryside facilitation and promotion.
- To stimulate employment as an economic and social strategy priority.
- Consolidation of interconnection between the labour market and educational strategies.

Positive rural development changes are forecasted due to Lithuania's accession into the EU accompanied by financial and technical support. Lithuania had formulated projects on rural and regional development measures that could be included into the Single programming document of Lithuania and into the "National Rural Development Project for the 2004–2006 period" (Table 1).

Table 1. Rural and Agricultural development measures 2004-2006 period (project)

Sources for measures		
European Agricultural Guidance and Guarantee Fund Guidance Section	European Regional Development fund or European Social Fund	European Agricultural Guidance and Guarantee Fund Guarantee Section
• Investment in agricultural holdings • Settling up of young farmers • Agriculture products processing and marketing improvement • Promoting the adaptation and development of rural areas • Forestry economy development • LEADER+ initiative measures for rural communities' leader training • Education	• Country tourism and uncommon trades support for new job creation in countryside • Support for agriculture water resource handling measures • Support of main services for rural businesses and rural population • Support for countryside's renovation, development and countryside heritage preservation • Professional education	• Farmer early retirement support • Less-favoured areas and areas with environmental restrictions • Support for environment and landscape saving farming methods – agro environmental protection • Agriculture purpose land foresting • Technical support, publicity and information services • Support for semi subsistent farms • Support for implementation of environmental standards

Findings

- Due to the East and Central European countries' integration into the EU, the cohesion of participating states' and regions' development processes are taking place. The same is true for understanding solutions of how the economic, environmental, cultural and social problems should be solved. A vision of integrated rural and regional development predominates in the EU agricultural and rural development policy. The rural development trend becomes one of the most important in Lithuania's agriculture policy.

- In Lithuania, the most important rural development problems are – low incomes, big and growing unemployment, big regional differences in living standards.

- The concentration of rural workforce in agriculture and low earnings from this activity predisposes both the need to diversify economic activities in rural areas and for agricultural restructuring. Only about 20% of those employed in agriculture have off-farm activities: agricultural processing and sales, tourism, crafts, other services, jobs, etc. Agriculture workers and small farm owners that do not have off-farm activities, usually have a subsistent lifestyle.

- The majority of Lithuania's rural population incomes are associated with agricultural activities, while its effectiveness depends on land quality, other farming conditions and

landscape, both earnings and the demand for rural alternative activities' vary strongly in different regions.

- To reduce the differences in living standards, an agricultural income support system (that suits EU requirements, for agriculture businesses, operating in less-favoured areas) was introduced in Lithuania. Less-favoured areas cover 1 612.2 thousands hectares or 48% of the state's agricultural land.

- The main solutions for the rural problems are: the provision of better judicial and economic conditions for direct investment into industrial and social infrastructure, in order to develop small and medium size businesses, youth and adult education, their re-skilling to suit local and regional labour markets; better utilisation of state support, that takes into consideration the rural district demographics and the economic situations and development possibilities.

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Part II: REGIONAL POLICY IMPLEMENTATION IN A CONTEXT OF FUTURE MEMBERSHIP OF LITHUANIA IN THE EUROPEAN UNION

By Mr. Algirdas Astrauskas, Under Secretary of the Ministry of the Interior

Abstract

This report is devoted to the presentation of the development of regional policies after the restoration of independence in Lithuania. In Lithuania the term "Regional Policy" is comprised of two components: 1) formation and implementation of the national regional development policy; 2) implementation of the principles of the European Union, which primarily means preparation for the administration of the European Union's structural funds. Special attention was paid to the establishment of EU requirements on the development of regional policies in the State. Until Lithuania becomes a member state of the European Union it has a challenge to make regional policy within the country more clear and effective, and at the same time to create conditions to efficiently absorb financial support from the EU.

Today, Lithuania is on the doorstep to joining the European Community, the necessity of an efficient regional policy in Lithuania is doubtless. After the restoration of independence in Lithuania, regional policy has passed some stages in its development and become expedient and purposeful. It is one of the most important state development priorities. Today, regional policy in Lithuania has a clear development vision and has identified its implementation strategy. Until becoming a member state of the European Union, Lithuania faces the challenge of making regional policy within the country more clear and effective. At the same time, conditions need to be created to efficiently absorb financial support from the EU.

Talking about regional policy, it should be said that at the beginning of 1995-1996 there was no such policy identified in Lithuania. There was no effective institutional infrastructure, as well as no legal basis for its implementation. At the same time, there was a number of indirect regional policy instruments, such as non-investment and investment programmes directed to the development of the Lithuanian economy. But, they were not related to each other and implemented via different governmental institutions.

The first time specific attention of the Lithuanian government was paid to regional policy was in 1998, when the Draft Lithuanian Regional Policy was adopted by the Government of Lithuania. The aims of the regional policy, as well as measures and implementation principles were defined. The Regional development division of the Ministry of municipalities and administrational reforms was created and authorized to co-ordinate the creation of regional policy and its implementation. In 1999, the division was transformed into the department and committed to the duty of the PHARE Economic and social cohesion programmes co-ordination and administration. In the same year, the National Regional Development Committee was created. The biggest emphasis in regional policy was placed on using EU pre-accession support through such instruments as PHARE, SAPARD, ISPA, etc.

A transition to the new planning and implementation mechanisms was most successful in those regions where the PHARE 2000 Economic and social cohesion programme had been implemented. Those are Klaipeda-Taurage, Utena and Marijampole target regions.

In 2000, the National Regional Development Institution functions (after the liquidation of the Ministry of Municipalities and administrative reforms) were committed to the Ministry of the Interior,

which also became responsible for the European Union negotiations of Chapter 21 “Regional policy and structural measures”.

In Chapter 21 of the Negotiations, Lithuania has made a commitment to prepare and approve the National Development Plan, which would meet the requirements for the Single Programming Document set out in the methodological documents prepared by the Commission (Regulation 1260/99/EC) by the end of 2003. The prototype of the current plan, the preliminary National Social and Economic Development Plan, prepared in 1999 was the main planning document for programming the PHARE Economic and Social Cohesion funds. In November 2000, the National development plan for 2001-2003 was prepared. The National Development plan 2002-2004 was the third attempt to elaborate a strategic document of the economic and social development of the country, covering a description of the current situation, respective strategies, priorities and tasks, as well as a preliminary financial plan. In 2003, the Single Programming Document 2004-2006 was prepared.

The first Law on Regional Development was adopted on 20 July 2000. It has foreseen the aims and objectives of regional policy, the institutional structure and the regional policy instruments.

By the decision of the Government of Lithuania, the Ministry of municipalities and administrational reforms committed to have a function of national regional development institution. At the same time, in the counties of the Republic of Lithuania, Regional development councils were created.

Preparation of the Law on Regional Development was built upon the presumption that the PHARE Economic and Social Cohesion component will be programmed and implemented in target regions in a decentralized way. Having moved over to the decentralized model for the management of this PHARE programme in 2000, the national regional development policy laid down in the Law has lost the main source of financing. This law had some inherent flaws – one of them being in conflict with the Council Regulation No. 1260/1999. It was necessary to revise national regional development policy and The Law on Regional development has been replaced with the new Law on Regional Development on 10 December 2002.

The aim of the national regional policy is to reduce interregional socio-economic disparities and sectorial disproportions within regions, as well as to promote sustained development throughout the state. The goals of the national regional policy are as follows: 1) to provide and implement state supports in problem areas, 2) to provide state support to projects being implemented in regions encountering specific regional and local problems in different sectors, 3) to create conditions for sustained long-term development of all regions.

Since 2000, the term "Regional Policy" is comprised of two components: 1) formation and implementation of the national regional development policy; the main aim of which is to reduce development disparities between Lithuanian regions; and, 2) implementation of the principles of the European Union, which primarily means preparation for the administration of the European Union structural funds.

The Ministry of the Interior implements the national regional development institution functions. National regional development policy and governmental administrational management is implemented in counties, is improving national regional administration structure, is participating in EU structural support programmes administration, directed to foster local and regional initiatives. Serious support in terms of regional policy strengthening will be done, such as the European Community initiative INTERREG III and preparing to effectively implement INTERREG IIIA directed to support cross-border activities. At the same time, a number of pre-accession support programmes are available

in Lithuania, such as the PHARE 2000 Economic and social cohesion, and the PHARE CBC 2002-2003 programmes, etc.

On 31 May 2001, the Government adopted the Resolution on the Administrative Distribution of Responsibility for Implementation of EU Structural Funds (SF). The Resolution laid the general legal and institutional framework for the future management of EU Structural Funds. According to the Government Resolution on Administration of EU Cohesion Fund in Lithuania, the managing Authority for all SF in Lithuania will be the Ministry of Finance. The Ministry of Finance is responsible for the EU structural policy in Lithuania.

Today, the national regional policy being implemented in Lithuania could be described as a clear, targeted activity of state institutions and other entities, that, through direct and indirect assistance measures, are aimed at differentiated effects on the socio-economic development of the regions of the state, with a view to reducing interregional socio-economic disparities and the disproportion of development in the regions, as well as promoting sustained and coherent development. This regional policy conception differs from those describing it, as one economic sector development in definite areas or only use of European Union financial support. Implementing this policy the Ministry of the Interior aims to reduce the gap in terms of economic and social development between the central and peripheral regions of Lithuania, where unemployment is highest, and where GDP per capita or foreign direct investment are lowest.

National regional policy is being implemented in statistical-administrative units called counties. At the same time, the law of Regional development provides a possibility to create regions that are at variance with administrative borders of counties. According to this provision of the law, the region of Ignalina nuclear power plant has been created in 2002. At the same time, a number of important documents have been prepared by the ministry, such as the Methodology of preparation and revision of existing regional development plans and the Regional development programme. The last one has been adopted by the Government of Lithuania. Under this programme, the preparation of regional development plans, consultancy of the regional administrations, project proposal preparations and international co-operation of the regions are going to be supported.

Session 3 Discussant Paper

By Mr. Hugh Laxton

No one seems to disagree with the need for an appropriate policy for development of rural areas. But, the historic debate about how best to integrate (or not) this policy with the more 'classic' policies for agriculture and regional economic development continues in the EU, at national and regional levels. While the 'ownership' of rural development policy may have changed over time, its political significance has only grown. The accession of 10 new Member States reinforces both its importance and the pressure for ensuring the policy is the right one. Both internally, between the sectoral and spatial interests of rural communities, as well as externally, between rural development policy and other development policies.

It is largely the historic mix of sectoral interests and regional objectives for development of rural areas that lies behind the complexity of the current EU policy architecture, which is often criticised by those living and working in rural areas. On the other hand, Member States (and regions) have almost complete flexibility to select from the 'menu' those measures most appropriate to their rural development priorities. Some changes to the rules on implementation, based on the early experience of implementing Rural Development Programmes, have been introduced already, but the Commission will continue to work with the Member States to see what more can be done to simplify the policy and its implementation. This will be among the main challenges for reform of the CAP and Regional Policy for the next period 2007-2013.

This presentation concentrates on support from the European Agricultural Guarantee and Guidance Fund (EAGGF) under the Common Agricultural Policy. The scope of rural development under CAP cannot, and does not try, to address all the economic and social issues facing rural communities. Any comprehensive strategy to address these wider rural development priorities will only be achieved by integrating the support available under the CAP with support from the European Regional Development Fund (ERDF) and the European Social Fund (ESF). The Objective 1 programmes offer this opportunity. DG Agriculture has indicated already the importance of allocating sufficient ERDF and ESF resources to address those issues beyond the scope of the CAP and to take account of the particularities of applying regional and social policies in rural areas, for example, cost of delivery. The idea of 'rural proofing' has been mentioned as one way to ensure that the needs of the rural society are considered in the preparation and implementation of all policies, which impact on rural areas.

Agenda 2000 established a distinct EU Rural Development Policy by bringing together various measures, many of which had previously been part of EU Structural Fund Policy, under the 'umbrella' of CAP, the so-called "second pillar". At the same time, it established the framework for linking this part of the CAP with EU economic and social cohesion policy.

The Rural Development Policy regulation[1] provides an integrated structure of 22 measures (5 additional measures[2] are provided for the new Member States during 2004-2006) serving principally rural functions and environmental functions, but also contributing to food production. These measures set out in the Rural Development regulation can be characterised to target three broad objectives. First, to restructure the farm sector to make it more competitive; second, to protect and

1. Regulation No. (EC) 1257/1999.

2. Treaty of Accession.

enhance the environment and landscape through changes to land management and production techniques and third, to improve the wider economic and social conditions for rural communities. Analysing the choices made by the EU-15 it can be seen that just over half of all EAGGF has been allocated to the second objective to support the environment. Around 40% is allocated to supporting the restructuring of the farming sector and only 10% has been provided for the broader development purposes in rural communities. However, there is a wide variation of this balance among the different Member States and, if one analysed the programmes at regional level, the variation would be wider still.

How is the integration achieved? First, it is important to note that the full scope of EU Rural Development Policy is available throughout the territory of the EU. Although, the implementation and financing of the measures are different, depending on whether a region is designated under Objective 1 or not. In the case of the three Baltic States the entire territory is Objective 1, and therefore, the delivery of these measures will be under the Objective 1 Single Programming Documents (EAGGF-Guidance) and the Rural Development Plans (EAGGF-Guarantee[3]). In EU-15 this architecture and the flexibility for Member States to develop regional, as well as national programmes have resulted in 68 RDPs and 89 Structural Fund programmes, which incorporate EAGGF rural development measures. The key to ensuring the coherence between these two instruments at Member State or regional level starts by ensuring that the strategy for the development of rural areas is not only the right one, but also the only one. It should underpin both programmes; there is no reason to prepare a different strategy for each programme. In addition, EU-15 is implementing 73 Leader+ programmes, whereby Local Action Groups (LAGs) establish local strategies for testing pilot or innovative ideas through a bottom-up approach. While the Leader+ initiative is not available to new Member States, the Treaty of Accession establishes a Leader-like measure, which will provide support for local communities to acquire the necessary skills, and where there is sufficient capacity already, a limited number of LAGs could be established.

As mentioned above, the EAGGF allocation between the 22 measures varies substantially among and within the current Member States. This menu approach not only demonstrates the ability to tackle priorities appropriately, it also reflects the positive link with EU regional policy and the possibility to fund certain measures from ERDF and ESF. This has the potential to increase the overall level of support directed towards rural development and allows the EAGGF 'envelope' to be used more intensively on measures, where other support is not available. Furthermore, it reflects the possibility for Member States to voluntarily modulate direct payments to make available additional resources for the four accompanying measures. In the examples provided in the slides, modulation only applies to the UK, which uses the additional resources for increasing expenditure on agri-environment measures. Some other Member States have also used the possibility to modulate their direct payments, but (as is provided for in the rules) they have not yet indicated to which of the accompanying measures the resources will be allocated.

So far this short presentation has referred only to what is provided for by current legislation and the Treaty of Accession. The latter reflects some of the reform proposals put forward by the Commission in January 2003. It is not the intention here to go into details of the reform proposals, but simply to highlight some of the key features related to rural development. It is most important to recall that these are *proposals only*. The Commission is hoping that agreement will be reached between the Member States in Council this month (June 2003) - in order to be able to meet the proposed timetable to start implementing the mid-term review proposals from 2004.

3. In the period 2004-2006 these measures will be financed from the Temporary Rural Development Financial Instrument (not EAGGF-Guarantee).

The overall thrust of the reform proposals - to make agriculture more market oriented and production better aligned to the demands of consumers particularly, in terms of food safety and the environment, reinforces the importance of rural development policy under the second pillar. In particular, three reforms proposed for the first pillar will have a critical impact on rural development policy. First, *decoupling* of support from production to a single farm payment will allow farmers to reorient their businesses and consider new developments, which can be supported by the rural development measures. Second, *cross-compliance* may require additional investment by farmers, which, if the Commission proposals are accepted, can be assisted by new rural development measures. These measures have already been agreed for implementation in the new Member States. Third, *modulation/degression* (currently a voluntary option) will provide additional resources from the first pillar to strengthen the rural development measures.

The Commission made clear from the outset that any mid-term review would not aim to propose fundamental changes to the rural development policy at such an early stage in its evolution. There has been some simplification to the implementation process as a result of the initial experiences of programme implementation, but Member States wanted to avoid major changes where possible. In fact, the Commission have proposed only to strengthen the policy with some additional options related to food quality, meeting standards and animal welfare.

As for CAP and rural development beyond 2006, the framework for the first pillar for post 2006 has been largely established already. The main principles of the financial perspective were agreed at the Brussels summit at the end of 2002. While, the future policy framework is largely set out in the proposals published in January of this year, although for some market sectors further proposals will be required. In the case of rural development policy (the second pillar) the framework has not been completed and will be closely linked to reform of the economic and social cohesion policies. The same is true for the financial 'envelope' although, subject to final agreement, the proposals for modulation would provide an additional amount of EUR 228 million in 2007 rising to EUR 1 500 million in 2013.

In considering the shape of the EU rural development policy post 2006 we need to continue to reflect on two key issues; the scope of the policy and its implementation and control.

Session 3 Discussant Paper

By Mr. Fritz Rembold

Executive summary

The transition process from a central planned to a market based economy has widespread implications for rural areas in CEEC.

During the last decades rural areas have been considered exclusively as a geographic space to allocate industrial conglomerates and large-scale state farms and co-operatives. Rural infrastructure was neglected to the benefit of investment in industries and other sectors of the economy. In the transition towards market economy principles and the withdrawal of the State from economic activities, most of these industries are now facing bankruptcy. As a consequence of the re-allocation of resources towards urban centres, rural livelihoods deteriorated dramatically in terms of access to social, physical and financial assets for the population. All countries in the region experience a very low degree of non-farm activities in the rural space with agriculture still accounting for a considerable share of employment and income opportunities. Among other implications, the decline in attractiveness has led to outward migration of the young and skilled, leaving behind an ageing population without long-term perspectives and reluctant to adopt innovative approaches.

The critical economic and social situations in the countryside require significant efforts by all stakeholders involved with the obligation for governmental entities to assume a leading role in providing the necessary political, institutional and conceptual framework.

EU candidates (hence to be member countries) received special accession funds to support regional and rural development initiatives including RNFE. However, the bulk of resources were allocated to agriculture and the farming sector. In terms of individual priorities, the highest importance has been accorded to the measures in favour of agricultural holdings, for processing and marketing and for farm diversification, with a clear preference for large size commercial agriculture.

Cross-sector, inter-institutional approaches and public-private co-operation are needed since the RNFE development of the country has to be conceptualized and integrated within the broader framework of rural development.

Additionally, local capacity building and stakeholder participation in decision making processes are considered to be pre-requisites for sustainability and, so far, there are still very few practical experiences with these matters in the region. Up to-date citizens especially in rural areas are still used to top-down approaches expecting ready-made solutions for their problems to be provided by the government and its institutions.

Consequently rural-regional development strategies, policies and projects have to take into consideration local needs and requirements, develop holistic, cross-sector approaches, integrate the notion of space including the rural-urban nexus, improve rural dwellers access to capital assets and hence increase the attractiveness of rural areas.

Alongside the necessary normative framework, capacity building, and stakeholder participation knowledge transfer, training and technical assistance is needed to raise awareness, build confidence and mutual trust.

Obviously the private sector including NGOs, and CSO will have to play a crucial role in these endeavours.

Brief assessment of related EU accession programmes

Example: SAPARD:

- The NSPs were characterised by descriptive instead of analytical/diagnostic thinking, consequently the strategy and operative parts were weak.
- Most CEEC still had difficulty in establishing and articulating priorities; this entailed delays in decision-making and the lack of involvement of stakeholder and actors, especially from the private sector.
- Weaknesses became apparent in inter-institutional communications and teamwork.
- Co-ordination difficulties are serious, especially where RD is not explicitly in one ministry at portfolio or at least directorate general level.
- As outlined, the bulk of the SAPARD measures and resources are targeted for agriculture and the farming sector. In terms of individual priorities, the highest importance has been accorded to the measures in favour of agricultural holdings, for processing and marketing and for diversification, with a clear preference for large size commercial agriculture.
- On the other hand most of the rural population is deprived from market opportunities; however, with less capital-and more labour-intensive and environmental-friendly production methods, access to markets for the poorer strata of the population could be opened up.

Recommendations and suggested approaches

1. **Complementarity/Cross-sector co-operation** among and between relevant line ministries/agencies.
2. **Programming** to establish long- and medium-term document plans on regional and national level according to identified priorities.
3. **Partnership** to include all socio-economic partners in decision-making and the implementation process.
4. **Sustainability** in terms of economic viability and ecological soundness.

Key measures

- Institutional development and organisational management.
- Human and social capital building (training courses, high level seminars and workshops, regional exchange programmes, research).
- "Ownership": Participatory – interactive approach in terms of defining together with the rural population the strategic measures to be implemented according to their needs, potentials and **absorption capacity**.

- Provision of advisory and information services (approach “visit & training”, demonstration plots and enterprises to obtain multiplication effects).
- Transparency in the use of financial resources, quality control, and participatory M&E.
- Corporate governance (Joint private-public sector endeavours).
- Preparation of area development plans.
- Strengthening land market development and related financial service provision.
- Greater labour market information (at a regional level) leading to counselling (*e.g.* Job Clubs).
- Work experience (particularly targeted at school-leavers).
- Vocational training especially in computing, tourism and services – also in terms of improved job-hunting skills, transferable skills and skills training of the long-term unemployed.
- SME training especially in self-employment.
- Paid public works.
- Support for seasonal work.
- Encouraging geographical mobility.
- Create credit schemes appropriate to individual communities, with an emphasis on low-cost operations managed by local stakeholders.
- Develop local leadership skills as a key aspect of RNFE programmes.
- Build on existing social and community networks.
- Support for marketing training and market development, including market research.

OVERALL CONCLUSIONS AND IMPLICATIONS

Summary, conclusions and policy implications

By Ms. Carina Lindberg

The final panel discussion, plenary comments and concluding remarks of the Seminar are summarised in this section of the report. First, the agricultural income situation across the region is discussed. Second, issues related to the high rates of registered unemployment in rural areas are debated. Third, rural and regional development problems and policies are discussed in light of EU accession. Finally, some broad policy implications are outlined drawing on the discussions of these complex cross sectoral issues.

Session 1. An overview of the agriculture and rural income situation and trends in the composition of income in Western Europe and the Baltic States

The issue of low, volatile and declining farm incomes has been at the centre of much debate in OECD countries. Some countries have responded to this problem by increasing support to agriculture through production subsidies, direct payments, as well as through programmes to facilitate structural adjustment. One of the main objectives' of government intervention in agriculture has been to raise incomes and consequently, to reduce poverty in rural areas. But, as farming becomes more heterogeneous in all countries, the idea that the "one size fits all" policy approach is no longer satisfactory. With a more diversified agriculture a better targeting of policy instruments is crucial.

The conceptual framework dealing with the incomes of rural households is based on several key elements; the definition of an agricultural household; the definition and measurement of incomes; and, the additional problems that may arise when applying this general framework to transition countries. At present, there is no internationally applied definition of an agricultural household. For EU countries, the EUROSTAT definition, *Income of the Agricultural Household Sector (IAHS)*, is the most widely used one. This definition of agricultural households includes those who work on agricultural holding and those who do not, but, reside in the household. At this juncture, the different EU member states have tended to use different variations of this definition depending on the specificities of the country and the availability of reliable data. The definition chosen by a country has a major bearing on the number of households covered and on the income picture that emerges.

Defining and measuring farm household incomes is becoming more and more difficult due to the increase in heterogeneity of farm structures, the sparcity of data, and differences in the composition of households. These conceptual difficulties tend to make cross country comparisons rather problematic. There are several approaches that can be used to get an estimate of net disposable income (NDI). While some countries derive estimates from the aggregate or macro-level using national accounts data, others take a microeconomic approach and derive NDI from household budget surveys, farm accounts surveys, or tax records. Another issue closely associated with the measurement of household incomes relates to the inclusion or exclusion of capital assets and changes in the value of these assets over time.

In most OECD countries, farm households have, on average, income levels close to those in the rest of society. However, research in OECD shows that the incidence of low income households is higher among farm households, than among other households, and the low-income gap is also wider for farm households than for others. While income from farming tends to be rather volatile, however, total farm household income is less so, due to the stabilising effect of non-farm income. The extent to which farm households engage in income generating off-farm activities alters the overall income situation of the household and makes it less dependent on agricultural activities. Opportunities for off-farm earning vary by country and region, and depend on several factors including, the structural

characteristics of the household, size and type of farm, rate of support, as well as the general economic environment. The different degrees to which farm households are dependent on agricultural activity, in turn, make them more or less affected by agricultural policy measures.

In the OECD area, for example, one-third of gross receipts resulted from some type of support in 2000-2002. However, a large share of the transfers due to agricultural policies does not translate into income gains due to transfer losses. In overall terms, the evidence from OECD countries suggests that there are serious difficulties in delivering income support to farm households through sector specific policies and measures. The main problems relate to lack of targeting, equity concerns and economic leakages. While policies do raise farm income, to some extent, and reduces variability, this tends to be achieved at a higher cost than necessary.

Another issue relates to how well this framework can be applied to transition countries, where the situation is more complex, as their farming structures are even more heterogeneous than those in OECD countries. In transition countries, farm types include corporate farms, family farms and subsistence and semi-subsistence farms. The structure of agricultural households is also different and can involve as many as three generations.

In the Baltic region, farm household income has fallen sharply during the transition period, due to the difficulties in the transformation process. However, in recent years the average farm household income has risen in Estonia and Latvia, due to the increase in farm size resulting in higher output and higher labour productivity on farms. Moreover, the sources of income are becoming more diversified with off-farm employment and social transfers representing a growing share of total income. The extent of this diversification varies widely between regions. But, low incomes and poverty are still a serious problem in rural areas, especially in Lithuania, because of the higher dependence on agriculture, slower transformation process, the nature of land restitution and lower opportunities outside agriculture. Another interesting observation is that the share of farm household income resulting from agriculture has decreased in Estonia, but increased in Latvia in recent years. In Lithuania, the share of income from social benefits/transfers has experienced the biggest increase, while income from framing has fallen.

Session 2. Developments in the labour market and factors affecting labour mobility in rural areas

Greater economic development accompanied by the modernisation of agriculture, has seen the continued and often accelerated outflow of labour from agriculture. This has given rise to high rates of rural unemployment in Estonia, Latvia and Lithuania, as well as in many OECD countries. The growth in registered unemployment in rural areas in the Baltic countries is likely to continue, with increased competition, following EU membership, accompanied by further structural adjustment in the sector. While most of the labour market and social policies have been reformed during the last decade, nevertheless, the success of these policies in reducing unemployment, especially among young people, in rural areas has been disappointing. High rural unemployment is at the centre of the current policy debate in the three Baltic countries and there is increasing focus on developing a more comprehensive policy framework that encompasses several policy arenas in order to resolve this pressing issue.

Labour markets in Estonia, Latvia and Lithuania, as well as in other transition countries, have all been strongly affected by the reorganization of farms that has taken place over the last decade. The share of employment on large-scale farms has declined, because large-scale farms have been partly liquidated and employment has moved towards household plots and emerging family farms. Furthermore, the remaining large farms have substantially reduced their labour use.

There are large regional differences in the Baltic labour market and, in general, unemployment tends to be lower in the big cities, regions with a diversified industrial economy and regions offering good opportunities for tourism and leisure. There has also been a reallocation of labour from agriculture and industry to the service sector. Agricultural production in Estonia, Latvia and Lithuania is relatively low, as are wages, and labour shedding from this sector is not taking place fast enough. The large outflow of labour from agriculture and rural areas has caused concerns about rural depopulation and even desertification in some areas. With this inevitable natural adjustment of labour markets, governments should not try to halt this process of labour shedding, but rather facilitate the adjustment process.

Labour mobility is a response to the trade-off between a range of "push and pull" forces in the economy. For example, the low level of education and skill set, of those leaving agriculture, limit employment opportunities in the general labour market. Moreover, many are elderly and have rather limited opportunities in terms of retraining. It was noted that the rapid rise in unemployment among young people in many rural areas is a growing cause of concern across the region. High rates of rural unemployment, in excess of 50% of the labour force in some regions, are at the centre of the current policy debate in the three Baltic countries. There is much focus on developing a more coherent policy approach to include agriculture, rural development, education and training in order to more fully integrate the rural unemployed (unskilled, young and long term unemployed) into the labour market.

There is an apparent paradox in both the demand for, and supply of labour. This is mostly due to an employment mismatch, where the characteristics of labour demanded is dissimilar to the characteristics of the available labour supply. This mismatch can be reduced by means of different labour market policies, focusing especially on education and training. It was emphasised that education is the most important precondition for the efficient allocation of labour and, consequently, for competitiveness and growth of modern economies.

To have a deeper understanding of labour mobility, participants examined the *decision-making process of individuals*. If people employed in agriculture consider changing jobs, they will most likely weigh the costs and benefits of leaving agricultural employment for other employment, either in rural or urban areas. Their decisions will be affected by several factors, including the relative income obtained in agricultural employment compared to other employment, the probability of finding alternative employment, the costs of moving from one job to the next and other benefits associated with employment in specific sectors. Integrating the employment choices of individuals into a *household decision-making* process provides further insights into this complex phenomenon. Households can allocate labour to more than one activity, and in so doing, reduces risk by diversifying their income sources, or access financial resources required in farming, which they cannot get through other financial institutions.

With stronger economic growth and investment in the Baltic region, employment opportunities are likely to increase, primarily in urban areas, however, with positive spill-over effects on rural areas. But, there are several factors that may continue to inhibit labour mobility in the region, despite the accelerated economic development of the region over the last decade. Some of the constraints include inadequate human capital, administrative/legal impediments, high personal risk aversion, availability of moderate housing, overall economic situation. Moreover, if one is moving to another country, there are additional constraints of dealing with a foreign language and culture, as well as being far away from family and friends.

Session 3. Rural and regional development policies

Policies and strategies to promote development of rural areas has become a high priority in many OECD and transition countries. In essence, intervention can be economically justified due to market failure or on equity grounds. There are broadly two types of market failures that potentially can hinder rural development: "traditional" market failures, that can exist in all locations, but for some reasons are exacerbated by rurality; and, market failures that are due to rurality in some way (*i.e.* space, distance and hence lack of agglomeration creates its own market failures). A better understanding of the underlying economic processes and linkages, that generate regional disparities, is fundamental in designing policies and strategies for rural areas.

The rural sustainable livelihoods model views rural development as an attempt to increase the "pool" of livelihood assets with which farm families construct their livelihood. In this context, the rural development paradigm uses three elements in order to redefine and revitalise the role of agriculture in rural areas: *broadening, deepening, and re-grounding.* The rural situation in the Baltic countries is different from that in most EU members, where the standard of living is higher and pluriactivity is prevalent in most rural areas. Agricultural employment is an important part of rural employment in the Baltics, especially in Lithuania, and therefore agricultural development is critically important for developing rural areas. Moreover, the situation differs between Estonia, Latvia and Lithuania, as reflected in the range of national rural and regional policies that are being implemented. At this juncture, all three countries are implementing the pre-accession measures, in particular, through the SAPARD programme. However, the institutional capacity for the different rural development instruments is still a limiting factor in the Baltic countries.

The experience of the LEADER programme in the EU, and more specifically, in Ireland, was taken as an example of a successful approach to developing rural areas. The experience and lessons from the programme indicate that the key elements of a local development approach are: an area-based rather than a sectoral development strategy; a competent local action group (LAG) to develop and manage the area-based development programme; a LAG that is representative, democratic and accountable; a LAG which places a high value on linkages and networks; a major emphasis on measures which enhance the capacity of people and institutions at the local level to manage their own development and; a strong emphasis on innovation and adding value to top-down and sectoral approaches. While the LEADER programme will not be implemented in the Baltics until 2007, a pre-LEADER programme will help the countries in developing local action groups.

It was noted that the LEADER programme may prove to be an important component of any future policy for rejuvenating rural areas in transition countries, it should not be seen as a quick-fix for all rural problems. The programme is a long term investment in capacity building for development and not a policy instrument in the broader set of farm and non-farm policy dimension. Human capital and capacity building through education and training have become important functions of the programme, and the degree of success of this capacity building will be decisive in order to achieve successful development.

It was noted that rural policies can be very costly, as resources have alternative uses in the economy. Rural and regional policies build on the assumption that spontaneous development is unsatisfactory and it is possible to correct this development at reasonable costs. Discussants recognised that the traditional range of national macro-economic and structural policy instruments of development needs to be complemented and reinforced by rural development strategies that have an area-based/spatial element, and a "bottom-up" method of implementation.

Policy implications

The three key questions raised and debated at the Seminar are:

- Why are rural (farm) household incomes lower than those of other households?
- Why are unemployment rates higher in rural areas than in other areas?
- What can be done by governments to reduce these disparities between rural and other (*i.e.* urban) areas?

In answering these questions, governments need to carefully identify and address the root causes of low incomes and unemployment, rather than the symptoms of market failures. Only then, can long-term solutions be created to resolving these problems. The twin problems of low incomes and high unemployment in rural areas also emphasises the critical need to develop a better understanding of the *economic linkages* that underpin regional differences in incomes. A combination of dynamic local initiative and top-down approaches are important elements in designing rural strategies that reduce income and welfare disparities between rural and urban areas and within rural areas.

It was emphasised that agricultural policy is not synonymous with rural policy. While they can be complementary and related to each other, nonetheless, agricultural policy is sector-specific, while rural development policy is multi-sectoral. In general, broad, output based measures to raise income should be avoided, as should production linked measures. Moreover, on-farm performance should be improved (skills, technology) and overall sector performance (food safety standards), with a view to improving productivity across the entire food chain. Greater attention also needs to be paid to the environment and to encouraging the provision of derived environmental benefits (create markets). Rural development policies should focus on specific measures to overcome market failures that are specific to the region, and should not be used to address general policy issues (*e.g.* tax policies, social policies, etc.).

Whatever problems and opportunities are identified, policy responses/objectives are best expressed in as specific and explicit terms as possible: What exactly do you want to achieve, over what time frame, and for when (whom)? Monitoring and adjustments should then be considered in light of the actual results and experiences. In their efforts to address specific problems, the key role of governments should still be to ensure a well functioning economy, with the overall objective to enable *economy-wide growth and development*. The focus would then be on macro-economic and structural policies that would allow markets to work, drawing on the strengths (and weaknesses) of countries' endowments:

- governance, institutions (public and private);
- responsible fiscal and monetary policies;
- systems of property rights and land markets;
- functioning capital markets (credit and investment);
- education and training;
- research & development, science & technology; and

- social safety nets and “social capital”.

The role for governments is to establish the overall operating environment in which businesses – including rural and farm businesses – can operate effectively and profitably. Within this overall policy context, any outstanding market failures could then be addressed by specific agricultural and rural measures. It was emphasized that governments will never be able to “fix” everything, but, individuals, private sector enterprises, NGOs and communities also have important responsibilities.

Much of the policy reforms and sectoral adjustment have already been achieved. Flexible, tailor-made approaches and a “whole of government” approach to further policy and programme activities can be expected to yield good results. Accession to the EU will provide new opportunities, but will not solve all the problems in rural areas. National governments must take the initiative to design their own tailor made and flexible strategies, taking advantage of the assistance available from the EU, FAO and other international organisations. Moreover, the continuation and expansion of the policy dialogue is crucial (*e.g.* with local stakeholders, other countries, private sector) and a key element involves promoting the empowerment of the human capital at local level.

ANNEX

Agenda

SEMINAR ON AGRICULTURE AND RURAL INCOMES, LABOUR MOBILITY AND RURAL DEVELOPMENT POLICIES IN ESTONIA, LATVIA AND LITHUANIA

10-12 JUNE 2003, TALLINN, ESTONIA

Introduction

The purpose of the Seminar is threefold. First, to discuss the low and volatile agricultural income situation across the region. Second, to debate the issue of high and rising levels of registered unemployment in rural areas. Third, to identify suitable rural and regional development approaches in light of these concerns. This is a very complex set of issues covering a range of macroeconomic policies (tax, labour, social etc.), sectoral policies (agriculture and food policies), as well as rural and regional development policies in all countries, both OECD and non-member countries. The objective of this Seminar is to get a better understanding of the underlying causes and linkages in Estonia, Latvia and Lithuania and to identify a set of approaches and policy instruments that could help resolve these problems.

The issue of low, volatile and declining agricultural incomes is a problem faced by many Governments in non-member countries. Several countries have responded to this problem by providing support to agriculture through input or output subsidies, as well as through structural adjustment programmes, such as investment support to facilitate modernisation and adoption of new technologies, early farmer retirement programmes, etc. Many of these programmes are designed to increase farm size and to enhance productivity and the competitiveness of those remaining in farming. Consequently, to increase and stabilise farm incomes. Other countries have focused on providing ever rising levels of market price support to agricultural commodities with the intention that this would resolve the agricultural income problem. As seen in some OECD countries, farm policies aimed at raising farm incomes are highly inefficient and inequitable, as most of the support goes to farm households where incomes are generally higher than the average income in the country in question. With ongoing changes in the sources of farm household incomes, traditional farm policies are becoming less and less effective, and better targeting of policies and policy instruments to rural and farm households is likely to be more effective and efficient in resolving the farm income problem.

High levels of unemployment, and indeed, significant levels of underemployment in rural areas continue to be a major cause of concern in many OECD countries, as well as in the three Baltic countries. With the accelerated economic development across the Baltic countries over the last decade, there has been substantial shedding of labour from primary industries, such as farming and fishing. The growth in registered unemployment in rural areas is likely to rise, with increased competition, following EU membership, accompanied by further structural changes especially in traditional rural enterprises. While most of the labour market and social policies have been reformed during the last decade, nevertheless, the success of these policies in reducing unemployment, especially among young people, in rural areas has been disappointing. High rural unemployment is at the centre of the current policy debate in all three Baltic countries and there is increasing focus on developing a more comprehensive policy framework that encompasses several policy arenas in order to resolve this pressing issue.

The recent evolution in rural and regional policies and the specific targeting of enterprise development are a direct response to the dual concerns of low incomes and high unemployment in rural areas in many countries. While traditional economic development policies concentrate more on achieving greater labour mobility and migration to urban areas, more recent thinking has focused on developing enterprises and consequently employment opportunities in rural areas. Rural areas differ markedly in their economic structure, natural and human endowments, demographic conditions and, thus, are affected to a different extent by socio-economic and policy changes at the national level. A better understanding of the complex processes involved and the implications of greater diversity are crucial for policy makers so that they can respond appropriately to the changing environment. Rural development with its multiple objectives requires a broad range of viable economic activities and cross-sector policies.

In order to achieve the objective and to facilitate an effective debate, officials from Ministries of Agriculture, Ministries of Social Affairs and Labour, Ministries of Economics and Regional Development will be invited to participate in the Seminar, as well as parliamentarians, local government officials, representatives of farmer organisations, researchers and academics. The main aim of this Seminar is to facilitate an objective and well informed debate in the issues of agriculture household incomes, unemployment and rural development in Estonia, Latvia, Lithuania, and to identify possible policy alternatives.

TUESDAY, 10 JUNE 2003

9:45-10:10 **Opening statements**
Mr. Tiit Tammsaar, Minister of Agriculture, Estonia
Mr. Ken Ash, Deputy Director, Directorate for Food, Agriculture and Fisheries, OECD

SESSION 1. An overview of the agriculture and rural income situation and trends in the composition of income in Western Europe and the Baltic States

Chair: Mr. Toomas Kevvai, Deputy Secretary General for Agriculture and Rural Development, Ministry of Agriculture, Estonia
Rapporteur: Dr. Michael Ryan, AGR/NME, OECD

This session will focus on recent changes in agriculture and rural household income and changes in composition of incomes. The participants will discuss and debate the opportunities, constraints and limitations facing households in rural areas within the context of ongoing structural changes and EU enlargement.

10:10–10:30 ***A conceptual framework for estimating agricultural household incomes in EU countries***
Prof. Berkeley Hill, Imperial College, University of London, UK

10:30–10:50 ***Farm household income situation in OECD countries: policy implications***
Ms. Catherine Moreddu, AGR/PTA, OECD

10:50–11:10 **Questions and comments**

11:10–11:30 **Coffee break**

11:30–12:15 **Presentation of country reports:**
Estonia, **Ms. Katrin Puhm**, Ministry of Agriculture
Latvia, **Ms. Ginta Uzulina**, Ministry of Agriculture
Lithuania, **Ms. Grazina Jalinskiene,** Ministry of Social Security and Labour and **Dr. Donatas Stanikunas**, Lithuanian Institute of Agrarian Economics

12:15–12:35 **Discussants:**
Mr. Antero Tuominen, Ministry of Agriculture and Forestry, Finland
Mr. Siemen van Berkum, Agricultural Economics Research Institute (LEI), Netherlands

12:35–13:00 **Plenary Session**

13:00–14:30 **Lunch**

SESSION 2. Developments in the labour market and factors affecting labour mobility in rural areas

Chair: Ms. Ginta Uzulina, Ministry of Agriculture, Latvia
Rapporteur: Mr. Wayne Jones, AGR/NME, OECD

In this session an overview of labour market, policies, as well as factors that influence mobility in the Baltic region will be presented and discussed. In addition, policy measures and instruments, which are currently implemented or planned, to promote efficient labour movement between different sectors of the economy, will be debated.

14:30-14:50 ***A framework for analysing labour mobility in agriculture and rural areas of transition countries***
Dr. Johan Swinnen, University of Leuven, Belgium

14:50–15:10 ***Factors that influence labour mobility between regions and countries***
Dr. Marek Góra, Warsaw School of Economics, Poland

15:10-15:30 **Questions and comments**

15:30-15:50 **Coffee break**

15:50-16:35 **Presentation of country reports:**
Estonia, **Ms. Kaili Järv**, Ministry of Social Affairs
Latvia, **Mrs. Aija Vucane**, Ministry of Welfare
Lithuania, **Mr. Martynas Storasta,** Lithuanian Labour Exchange

16:35-16:55 **Discussants:**
Dr. Waldemar Guba, Agriculture Policy Analysis Unit (SAEPR/FAPA), Poland
Dr. Tomas Ratinger, VUZE Institute, Czech Republic

16:55–17:30 **Plenary session**

19:00–21:00 **Cocktail**

WEDNESDAY, 11 JUNE 2003

SESSION 3. Rural and regional development policies

Chair: Dr. Raimundas Duzinskas, Lithuanian Institute of Agrarian Economics, Lithuania
Rapporteur: Ms. Carina Lindberg, AGR/NME, OECD

The growing pressures from high and rising levels of unemployment and low incomes in rural areas arises due to structural changes in the traditional industries and lack of new employment opportunities. Therefore, this session will identify and debate the different experiences in rural and regional policies in the Baltic States and OECD countries. In this session, the different approaches of countries, to increase incomes, to reduce unemployment, to create suitable employment are discussed. Also, policies and instruments will be discussed that promote the development of enterprises and infrastructure in rural area.

9:00–9:20 ***Developing an integrated policy for rural and regional areas in the Baltic countries***
Dr. Ewa Rabinowicz, Swedish Institute of Food and Agricultural Economics, Sweden

9:20–9:40 ***Strategies for local development in rural areas***
Prof. Joseph Mannion, University College, Ireland

9:40–10:00 **Questions and comments**

10:00–10:20 **Coffee break**

10:20–11:05 **Presentation of country reports:**
Estonia, **Ms. Riin Saluveer**, Ministry of Agriculture
Latvia, **Ms. Marita Baltina**, Ministry of Agriculture
Lithuania, **Dr. Donatas Stanikunas,** Lithuanian Institute of Agrarian Economics

11:05–11:35 **Discussants:**
Mr. Hugh Laxton, DG Agriculture, EU
Mr. Fritz Rembold, FAO-SEUR

11:35–12:30 **Plenary session**

12:30–14:00 **Lunch**

SESSION 4. Field Trip: Estonian experience of the impact of labour and rural/regional policies in a selected region

The purpose of the field trip is to see how policy measures have resolved unemployment, low income and other problems in agricultural regions. The field trip may also include a visit to a region, where these problems have not yet been solved.

14:00–19:00 Field trip (information to be provided at the Seminar)

THURSDAY, 12 JUNE 2003

SESSION 5. Policies to facilitate the development of a sustainable agricultural sector and rural areas

Chair: Mr. Ken Ash, AGR/DO, OECD

This session will summarise the existing and planned policies in the three Baltic countries, in particular, the advantages and weaknesses of these policies. The main outcome of this session will consist of conclusions and recommendations for Baltic policy makers to consider, and possibly implement in their respective countries.

9:30–10:15 **Summary: the three rapporteurs will provide a synthesis of the discussions from Sessions 1, 2 and 3**

10:15–10:45 **Comments (Heads of Delegations of the Baltic countries):**
Estonia, **Mr. Tiit Tammsaar**, Minister of Agriculture
Latvia, **Ms. Ginta Uzulina**, Ministry of Agriculture
Lithuania, **Mr. Jonas Panamariovas**, Under Secretary, Ministry of Agriculture

10:45–11:00 **General comments**

11:00–11:20 **Coffee break**

Chair: Mr. Ruve Schank, Counsellor, Ministry of Agriculture, Estonia

11:20–11:45 ***Policy options for effective agriculture and rural development in the Baltic States***
Mr. Ken Ash, AGR/DO, OECD

11:45–12:15 **Final comments and concluding remarks (Experts/Participants)**

12:30 **Press conference**

SEMINAR ON AGRICULTURE AND RURAL INCOMES, LABOUR MOBILITY AND RURAL DEVELOPMENT POLICIES IN ESTONIA, LATVIA AND LITHUANIA
10-12 June 2003, Tallinn, Estonia

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OECD PUBLICATIONS, 2, rue André-Pascal, 75775 PARIS CEDEX 16
PRINTED IN FRANCE
(14 2003 11 1 P) ISBN 92-64-10428-3 – No. 53225 2003