

AGRICULTURE IN TRANSITION COUNTRIES AND THE EUROPEAN MODEL OF AGRICULTURE: ENTREPRENEURSHIP AND MULTIFUNCTIONALITY

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INTRODUCTION

Objectives

This paper has two main objectives. The first one is to show what are the key-issues and constraints of agricultural development in transition countries and the second to assess how they can be fitted into the current framework of agricultural and rural development policies of the EU. By agriculture in transition we essentially mean the evolution of agriculture in the European transition countries, that is Central and Eastern European countries (CEECs). Moreover, we look at this evolution in a EU perspective that is considering the opportunities as well as the constraints the CEECs accession is going to imply. The outcome of this twofold analysis is to derive some consequence and implication for the specific case of the two Croatian counties of Zadar and of Šibenik-Knin. In particular, general concepts and perspectives should help in identifying the strategic lines for local agricultural and rural development within the current and future EU framework.

Overview

The first section of the paper will therefore deal with an overview of the main and general agricultural issues in transition countries emerging in the literature, how they are connected to wider rural development constraints and which instruments the EU have already put in place. Then, the second section will more deeply shift toward the definition of the main concepts and strategic lines of the current EU policies in agriculture and for rural development. The guiding idea is that the key objectives of agricultural and rural development policies for the transition countries have to fit into these general lines and have to be able to apply for the respective instruments. These are actual opportunities conditioned to the ability to create locally the appropriate entrepreneurship required by this new vision of the agricultural production and, mainly, by its multifunctional nature. The third section will try to introduce some basic concepts and definitions related to this new vision of the multifunctional farm as rural enterprise and, consequently, of the farmer as rural entrepreneur.

AGRICULTURE IN TRANSITION

Many recent works have reviewed and analysed the critical problems of agricultural development and transformation in the European transition countries. Despite the relevant differences that can be detected between and within each country, it emerges that most crucial issues are substantially common. This happens because the transition process has invested rural areas following similar patterns. Firstly, the economic and institutional transformation process in the CEECs has severely affected rural areas and livelihood of rural people. Secondly, rural areas have registered a general and significant decline in output and employment in early stages of the process. Finally, in most CEECs the rural economy is still lagging behind in recovery and employment creation with respect to the urban areas.

Moreover, the EU Commission has recently (June 1999) approved a specific instrument for financing development programmes in agriculture and in rural areas in the 10 accession countries² (Special Accession Programme for Agriculture and Rural Development: SAPARD). All the 10 accession countries have already submitted a proposal for support under the SAPARD in the spring of 2000 and this documentation represents an important reference to detect the main problems to be tackled. These proposals contain, among other things, a list of weaknesses and strengths of the rural economy, and of the agricultural and agri-food sectors, as perceived by the authorities of the countries themselves. Swinnen *et al.* (2001) provide a detailed review of the proposals as well as of the existing literature on the topic. This review is synthesised below.

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² The 10 accession countries are: Hungary, Latvia, Slovenia, Bulgaria, Czech Republic, Lithuania, Slovakia, Poland, Estonia, Romania.

Crucial issues of agriculture and rural areas in transition countries

A first issue has to do with the farm structure. Existing farms are usually small and, in particular, conditioned by fragmented plots. This problem is strongly related to the transition process itself since the privatisation and the land reform still leave the property rights uncertain in many cases. This uncertainty also strongly hampers the development of an efficient land market, which could allow a re-organisation of the production structure. In any case, whenever the land market would function correctly, many family-farms would be limited in extending their land capital by great obstacles in the access to credit. The current functioning of the credit market makes the credit itself unaffordable by most farms in many rural areas. Appropriate institutional innovation (subsidising loans, microcredit, etc.) would strongly reduce this major problem.

A second issue is the low level of labour productivity which inevitably implies low income level in agriculture and in rural areas as a whole. Two main points emerge in this respect. Firstly, farm technology is generally considered obsolete and under-mechanised. Again, easier access to credit would foster agricultural investment and consequently improve the technological level. Secondly, low output prices are very often the consequence of great difficulties of the small farms to enter the agricultural markets. On the one hand, the absence of appropriate institutional arrangement (up- and downstream contracting, cooperatives and/or associations) makes the rationale organisation of agricultural supply quite difficult, especially when referring to typical and local products. On the other hand, however, the quality of products is low or at least not enough standardised particularly with respect to the international markets.

A third strategic issue, in this sense, is the ability to reorganise the whole agri-food generating a tighter connection between the farmers and the industrial transformation and/or the market-chain. However, the agri-food sector itself shows relevant weaknesses. In general terms, there are too many and fragmented plans operating at an inefficient scale. At the same time, the investment rate is low and, consequently, the technological level is poor.

In any case, however, these agricultural weaknesses are interlinked with the general characters of the whole rural economy. Agriculture will hardly be able to recover higher level of productivity and market performance if the rural economy does not get over some general depressing factors. The first one is the low general level of income, which in turn depresses the local demand and the investment rate shortening the capital for new investments or firms. Secondly, population is significantly ageing due to selective out-migration of young people toward urban areas. This also reduces the average level of education as well as upgraded training and skills. Finally physical infrastructure is generally considered poor and also inappropriate and outdated for an easier access to markets and connection with the urban areas. Considered separately, these issues may also be present in Western-Europe rural areas. In transition countries, however, they generally appear simultaneously and this induces a self-reinforcing process of increasing divergence from the urban regions.

Constraints in reallocation of labour

The interlinked problems of the farm production and of the whole rural economy induce a perverse effect on the adjustment and recovery process. On the one hand, modernisation and rationalisation of the agricultural sector would imply an increase in labour productivity and a consequent decline in labour demand. However, the weakness of the rural economy already induces high unemployment rates in rural areas, and often of a structural nature. Therefore, the reallocation of labour is a key-aspect in interpreting the transformation as well as the perspective of both agriculture and the whole rural economy. Differently from most Western European countries, agriculture is still the main sector (especially for employment) in most rural areas in the CEECs. Labour should be reallocated from agriculture to other non-agricultural activities but shouldn't move from rural to urban areas thus provoking out-migration. Therefore, a rapid growth of local non-agricultural activities and firms is of strategic relevance.

Here, we want to detect briefly the main evidence about how reallocation developed during the transition and which main constraints hamper the creation and development of new non-agricultural businesses and enterprises. During the first five years of transition, great differences in agricultural employment decline have been observed across CEE countries: around -50% in Czech Republic, Slovakia, Hungary and Estonia; a lower decline in Poland, Slovenia and Latvia (between -10% and -20%); a significant increase in some other countries, such as Romania, Lithuania and Bulgaria. Moreover, great differences can be also observed within the countries themselves. It is difficult to explain this strong heterogeneity. In general terms, two classes of explanation can be advanced. On the one hand, structural differences among the agricultural sectors in the pre-reform period could have strongly affected the agricultural employment decline during the transition. On the other hand, the transition process itself and in particular relevant differences in the reform policies can have played a major role.

The combination of these two different aspects actually guided the main forces of agriculture transformation. First of all, they generated a different decline in agricultural terms of trade due to different price and trade liberalisation. This in turn generated a different reduction in agricultural profitability and labour productivity,

therefore causing a different reduction in the demand of agricultural labour. At the same time, the sharp increase in relative prices of other agricultural inputs induced a substitution of these inputs with labour, partially, or totally, offsetting the mentioned decline in labour demand. Beyond the reform policies, these two opposite effects on agricultural labour demand has had a different impact according to the original structural characters of the farm and of the agricultural family. In fact, in poorest countries household farming also provided food and social security therefore limiting the labour outflow if compared to countries with state provision of social security (unemployment benefits, pensions, etc.). The farm structure itself played a key-role. Where the large-scale farms remained dominant (from state and collective farm to independent company) the outflow was more intensive while, on the other side, the shift from state-collective farms to individual-family farms induced strong gains in labour productivity and reduced outflow of labour.

However, another possible explanation relies on the fact that agricultural employment remains stable, or increases, where there are not significant alternative job opportunities. This would imply, on the one hand, that part of agricultural employment is indeed hidden unemployment. On the other hand, that lower agricultural employment reduction should be associated with higher unemployment rates. Table 1 shows, however, that this regularity can be hardly detected; in any case, this can happen because strong outflow from agriculture could itself increase the official unemployment rate. Studies on what happened to labour leaving agriculture (Swinnen *et al.*, 2001) are hampered by the little and heterogeneous statistical information available. Data about the Czech Republic provided by the OECD (OECD, 1999) would indicate that only 5% of the real labour outflow from agriculture became unemployed and most remained in the rural areas rather than migrating to urban ones. 50% retired prevalently remaining in the rural areas themselves, while 45% found a new job in other sectors but mainly (75%) moving to the urban areas. Therefore, the process slightly increased the unemployment level but strongly fostered the process of selective out-flow from the rural regions.

It is hard to say if these figures can have a general validity across all the transition countries; however, there is some evidence that the contribution to unemployment by agricultural labour decline has been quite higher elsewhere. In any case, when referring to a specific regional-local context, it is crucial to understand how and how intensely the labour re-allocation proceeded. If the process developed slower and has still to be completed, a significant level of hidden unemployment in agriculture could be detected and a further out-flow could be expected whenever labour productivity gains will be forced by the market. In addition, this also implies the need of creating alternative job opportunities in the rural context itself, to avoid a rapid and selective migration to the urban centres. The creation of alternative jobs in the rural context, however, mainly means creation of new businesses and stronger incentive to entrepreneurship and self-employment.

Table 1: Unemployment rate and change in agricultural employment in 10 accession countries and Albania

	<u>Unemployment</u> (1998,%)	<u>Agricultural employment</u> Δ 89 – 95 (%)
Albania	16.9	-3
Bulgaria	16.0	12
Czech Rep.	6.1	-56
Estonia	5.0	-44
Hungary	9.5	-57
Latvia	9.2	-8
Lithuania	6.9	12
Poland	10.0	-17
Romania	10.3	24
Slovakia	15.6	-49
Slovenia	14.6	-20

Source: Swinnen *et al.* (2001)

NEW RURAL ENTREPRENEURSHIP AND BUSINESS DEVELOPMENT IN TRANSITION COUNTRIES

According to the discussion above, the agricultural transition is essentially linked to the evolution of the whole rural economy in the local context. Agricultural labour reallocation is the main factor of the tight linkage. Preventing selective out-flow from the rural to the urban regions implies creating new job opportunities in the rural context. Self-employment, microbusiness development and new entrepreneurship is

therefore a key-issue (Phillipson, 2001). Moreover, transition itself have pushed self-employment due to overall economic deregulation, increase in unemployment and decline in provision of social services.

Several analyses and some studies based on firm-level survey (Swinnen *et al.*, 2001; Sarris *et al.*, 1999; Rizov *et al.*, 1999; Mathijs and Vranken, 1999; Bojnec *et al.*, 1999) have pointed out that the key-factors for new entrepreneurship and creation of new businesses in rural areas can be summarized in four categories. It emerges that in rural areas in transition the main constraints to self-employment in agriculture as well as in other sectors can be referred to:

- Human capital: although individual characteristics and motivation are always a crucial aspect, key-factors seem to be education and age. Creation and survival of new businesses is associated to young and highly (in relative terms) educated entrepreneurs. On the other hand, skillness in terms of previous experience in former state-collective farms or firms is not so relevant in starting individual enterprises.
- Physical capital and finance: the availability of physical capital for business start up and development depends on original ownership of machinery, buildings and livestock, especially where capital markets are imperfect, and on the functioning of the credit market. Where relevant innovations on the credit market are lacking, some alternative arrangements can allow the new firms the access to capital. One of them is the availability of contracts with upstream processors especially for the adoption of new technologies; another one is the presence of Foreign Direct Investments (FDI) that foster innovative business arrangements and vertical coordination.
- Market institutions: as mentioned above, institutions of vertical coordination have substituted market imperfections in some cases. A particular positive effect on new businesses are due to contracts with upstream processors that facilitate access to credit, to new inputs and new technology, but also relieves cash flow constraints and uncertainty. Also crucial in rural areas is the membership of cooperatives or companies that facilitates the access to marketing opportunities and information. In many cases this new institutional organization in the rural context also allows former production cooperative taking up new roles.
- Policy environment: during transition the policy environment have had a crucial impact on several aspects for business start-up in rural areas. The main aspect is the set of privatisation and decollectivisation regulations whose level of complexity is inversely related to the real chances of taking up new initiatives. We particularly refer to actual land reform and property rights security. A second crucial aspect is macroeconomic stability that affects new rural enterprises mainly in terms of low interest and inflation rates; moreover, macroeconomic stability greatly affect the climate for inflow of FDI.

Again, many mentioned issues can be detected also in most Western Europe rural areas. However, in the CEECs they often appear simultaneously and with higher intensity, and their interaction provides a much more consistent constraint to the creation of new activities. Moreover, rural areas in Western Europe can refer to existing policies of the EU specifically directed to these kind of problems and they have already acquired those procedures and institutions aimed to implement those policies effectively and consistently. This capacity has still to be developed in the Eastern countries and have to be designed according to the new perspective of the European agricultural and rural development policy.

THE (NEW) EUROPEAN MODEL OF AGRICULTURE

The main issue, but also opportunity, the agriculture and rural areas in transition are going to face is to fit their on-going transformation into the requirements and instruments of the Common Agriculture and Rural Development Policy. Most CEECs already applied, or are going to apply, for the accession to the European Union, and 10 of them are already implementing policies directly funded and designed by the European Commission aimed to facilitate the application of CAP principles to the new entrants. In this respect, we will deal with the SAPARD programmes later in this section. Before that, we want to outline briefly the new directions of the agricultural and rural development policies in the EU, according to the so called European Model of Agriculture, since they inevitably has to represent to target of any agricultural transition policies.

The background

Buckwell (1998) carefully describes the process of review of the Common Agricultural Policy (CAP) carried out by the European Commission in the second half of the ninties. The Commission position was formed on the base of the two main constraints and challenges facing the CAP in the new century: the need for the EU to respect the commitments made in the Uruguay Round (GATT/WTO) Agreement on Agriculture; the prospect of EU enlargement to Central and Eastern Europe. The main conclusion was the basic strategy to "continue the 1992 reform process and move towards a more integrated rural policy". This latter means to move the whole basis of support away from being a sectoral policy for agriculture based on commodity price support, towards being a more integrated policy for rural areas. These considerations apply *a fortiori* to most CEECs where there is a gross over-manning of agriculture, both in the form of very small holdings, and

amongst employed workers or co-op members on larger holdings. It will not be possible to achieve satisfactory living standards for these people from agriculture alone.

This is in the essence the idea which have emerged in the last five years from a variety of sources in Brussels and in the member states. The most intense flowering of the need to move to a more integrated rural policy was expressed at the Cork Rural Development Conference in December 1996. According to the Cork Declaration there produced, sustainable rural development must be put at the top of the agenda of the European Union, and become the fundamental principle which underpins all rural policy in the immediate future and after enlargement. Rural policy has to be by definition multi-sectoral and, given the diversity of the Union's rural areas, must follow the principle of subsidiarity. It must involve all the relevant sectors and economic activities in the specific rural context and has to be as decentralised as possible and based on partnership and co-operation between all levels concerned (local, regional, national and European). The emphasis must be on participation and a 'bottom up' approach, which harnesses the creativity and solidarity of rural communities.

The farming industry, which was in the minority at Cork, plus the regional development interests did not feel part of this conference and have resisted its conclusions. Nonetheless, the Commission has continued to argue the case for what calls the European Model of Agriculture (EMA). This new concept emphasises the dual function of agriculture which supplies not only food (a market good) but also the non-market environmental and cultural landscape services. The EMA is clearly and synthetically described in Vanderpoele (2001). It became the cornerstone of the EU agricultural policy in the European Council in Luxembourg in 1997. It is a policy statement about the unity between society, landscape and agriculture which has become an important tool, rather than a new normative framework, for agriculture and rural policies in the future. It is closely linked with the concepts of the multifunctional character of agriculture, of sustainable agriculture and of multisectoral rural development.

Since EMA is such a broad concept, it is difficult to define. Let's say that the core element is a balance between economic, social and ecological values aiming, for the purpose of economic and social cohesion of the enlarged union, at:

- a competitive agriculture where possible (food function);
- at maintaining agriculture where necessary for the protection of the countryside (environmental function);
- at increasing the viability and the quality of life in rural areas (rural function).

According to this basic idea, the change in the architecture of the CAP have to be build on two pillars: traditional market policies (Common Market Organisations = CMO) and rural development policies with the commitment in medium to long term of fundamentally redirecting financial resources from commodity support to rural development.

The PAC and the rural development policies after Agenda 2000

Agenda 2000 defines the changes in the CAP which the Commission argues are necessary to take the EU through to the year 2006. During this period the next round of multi-lateral trade talks will presumably have been completed and the first wave of CEECs will have been admitted into the Union and starting whatever transition period is agreed. Two other important elements of the context of the proposals for agriculture in Agenda 2000 were the Union's structural policy and the financial perspectives. Essentially the proposals for the structural policy were to simplify the six objectives down to three and to concentrate structural resources on the poorest regions and those with most intense difficulties. This creates a conflict with the proposed territorial broadening of rural development policy advocated above. However, agriculture still dominates the EU budget. The Agenda 2000 proposals were that the present parameters of the Union's finances, including the agricultural guideline, should be rolled forward, unchanged, to 2006.

The principal elements of the agricultural proposals fall into three categories (Buckwell, 1998), that can be generally described as follows:

- *the changes in Common Market Organisations (CMOs):* the intervention prices for arable crops, beef and milk are to be reduced from 2000 by 20%, 30% and 15% respectively. In all cases the price cuts will be 'compensated' by what are termed 'direct payments' or 'direct income payments'. In the beef and dairy CMOs, a new device is proposed, to devolve to the Member States the responsibility for distributing part of the compensation.
- *a new set of horizontal measures applying to all CMOs:* three new concepts are proposed to apply to all direct payments under the CMOs. These are payment ceilings, modulation and cross compliance (or eco-conditionality). The first is a redistribution measure. It proposes that total direct payments per farmer between 100,000 and 200,000 ECU be only partly (80%) paid, and for amounts above 200,000 ECU only three-quarters be paid. The proposal on modulation is also apparently aimed to limit the payments to certain 'less deserving' farms. For farms which employ fewer than some (member state defined) labour norms, the member state may choose to cut the direct payments by up to 20%. The

third horizontal measure is the requirement for member states “to take the environmental measures they consider appropriate”. If farmers do not respect such conditions the member state may impose sanctions “proportionate to the seriousness of the ecological consequences of not observing mandatory environmental requirements.”

- *the rural development measures:* this is a relevant simplification and integration. Nine existing structural regulations directed towards rural areas, including the three MacSharry accompanying measures, are condensed into one. Two types of rural development (RD) actions are defined: 1) the 1992 accompanying measures (early retirement, forestry and agri-environment) plus redefined less favoured area measures; 2) measures concerning modernisation and diversification.

There is actually a four component of the agricultural and rural development policy according to Agenda 2000. This is the provision for pre-accession aid to the Central and Eastern European Countries through financing country-level agricultural and rural development programmes (SAPARD). Before going into a detailed analysis of the SAPARD programmes it must be stressed that this revision of the CAP should create the architecture for policy to switch in the way suggested by the EMA concept. However, the continuation of the same budgetary guideline for the structural funds means that there are rather restrictive limits on the rate of growth in structural expenditure, whereas the agricultural budget can continue to grow at up to 74% of the growth of EU GDP itself. This also implies that the first pillar of the CAP still cover almost 90% of the whole CAP budget while the second pillar (on whose the EMA concept mainly relies) continues to play a minor role (Sotte, 1999).

Moreover, a relevant part of the budget of the rural development policy is indeed covered by traditional, i.e., pre-agenda 2000 measures. In fact, the total RD funding is over 100 bio € for the period 2000-2006 or 14.3 bio €/year, of about which half EU, half national source. According to the data currently available at the Commission-DGVI (Pasca-Raymondo, 2001), the EU part Guarantee section amounts to 4.6 bio €/year and Guidance section to 2.5 bio €/year; the Guarantee covers the accompanying measures that on EU average account for 49% of the total RD funding. Agro-environmental measures and LFA (Less Favoured Areas /AER (Areas of Environmental Relevance) by themselves covers respectively about 25% and 15% of total funding (figures 1 and 2).

Figure 1: Total Public Expenditure in the EU (EAGGF) for Rural Development (Mio. €)

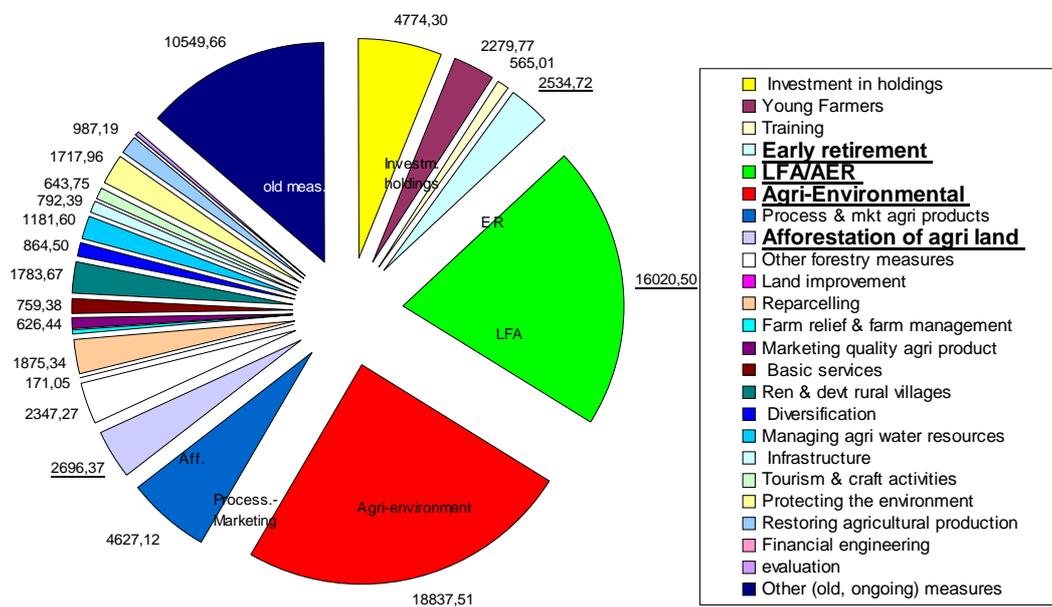
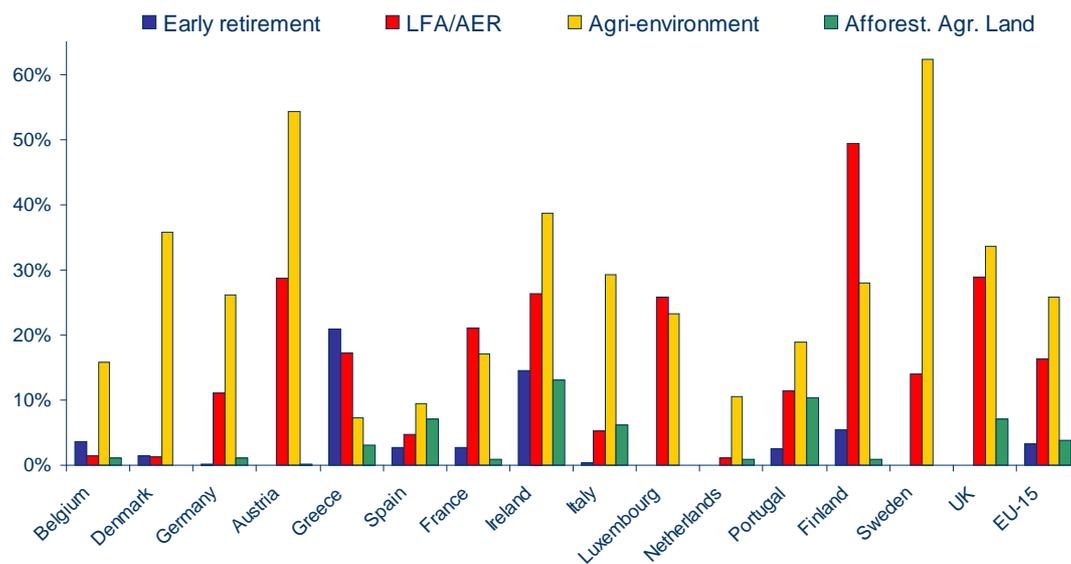


Figure 2: Share of individual accompanying measures in rural development EU funding



Source: DG VI, Pasaca-Raymondo (2001)

The SAPARD programmes

A fourth and new part of the Agenda 2000 proposals about agricultural and rural development policy provides for pre-accession help to the applicant countries of Central and Eastern Europe. All 10 accession countries have submitted a proposal under the Special Accession Programme for Agriculture and Rural Development (SAPARD) to the European Commission in the spring of 2000. The funding and assistance offered by the EU is for two main purposes: to help the applicant countries implementing the *acquis communautaire* concerning the CAP, and to help modernize and adapt their agricultural sector and rural areas. The underlying idea is to make the accession countries rapidly fit into the new concepts of the second pillar of the CAP and, therefore, the new concepts of the EMA. The measures offered are essentially the same rural development measures offered in the existing EU policy for rural areas according to Agenda 2000, including farm restructuring and land re-parcelling.

Support under SAPARD is granted on the basis of a single agricultural and rural development 2000-2006 programme *per* applicant country reflecting priorities established by national authorities. Differently from other pre-accession instruments (PHARE and ISPA), under SAPARD the national authorities assume entire responsibility through fully "decentralised management". The SAPARD programmes are to a large extent comparable with Member States' agricultural and rural development programmes. As these, the Commission co-finance the programmes; the assistance provided is expected to be co-financed by the EU at a rate of 75%. Before granting, a set of provisions covering aspects relevant to the proper use and accountability of funds have to be negotiated and agreed. Accordingly, a Multi-annual Agreement between the Commission and any country have to be established. Moreover, granting is conditional on the activation in each applicant country of an unique Agency capable and responsible of implementation of the SAPARD according to the agreement (European Commission, 2001).

Total financial support from the Community amounts to over 0.5 bio €/year in the period 2000-2006 (0.529 in 2000, 0.540 in 2001). In any case, funding is lower than the other pre-accession programmes: in 2000 1.59 bio € for PHARE and 1.06 bio € for ISPA. The SAPARD regulation entered into force on June 1999. All 10 applicant countries submitted the national plans within January 2000. All have been considered admissible by the Commission by spring 2000. On 29 November 2000 the Commission approved the final version of the text of the Multi-annual agreement. The first to sign was Bulgaria (18 December 2000). By March 2001 all 10 agreements have been signed but, however, by the end of 2000 no national agency was ready to receive funds. Currently (June 2001), two countries (Bulgaria, Estonia) have received funds but the Commission expect that most countries should be able to have grants by the end of 2001. According to the SAPARD regulation, the funds (provided by the Guarantee section of the European Agricultural Guarantee and Guidance Fund, EAGGF) have to be distributed among applicant countries according to: farming population, agricultural area, gross domestic product per capita and specific territorial situation. The most important criteria, however, are agricultural area which account for 60% and farming population (30%). According to these principles, an indicative allocation by beneficiary country of the maximum annual amount in 1999 prices is reported in table 2 (see Swinnen *et al*, 2001 for details).

Table 2: SAPARD: indicative allocation by beneficiary country of the maximum annual amount in 1999 prices

Country	Amount (in thousands euro)
Hungary	38,054
Latvia	21,848
Slovenia	6,337
Bulgaria	52,124
Czech Republic	22,063
Lithuania	29,829
Slovakia	18,289
Poland	168,683
Estonia	12,137
Romania	150,636
TOTAL	520,000

Source: European Commission (2001)

Each national SAPARD proposal contains, among other things, a list of weaknesses to be targeted. These are reviewed for the 10 applicant countries in table 3. The plan is divided in 15 measures similar to those available to EU Member States under the Community co-financed agricultural and rural development programmes. Only few measures eligible in the Member States are not eligible under SAPARD: setting-up of young farmers, early retirement and less favoured areas. It must taken into account, however, that these three measures, in particular early retirement and less favoured areas, cover an important part of the rural development funding in the current EU members (see figure 1). Three measures are dominant in most applicant countries (69% of total EU funds for the SAPARD): processing and marketing, investment in agricultural holdings, investment in rural infrastructure. On the contrary, two measures (setting up farm relief and farm management services, establishing and updating land registers) have not been included in any programme. Although they play a crucial role in current member states, agro-environmental measures seems actually accessory in most proposed SAPARD plans. It appears that environmental concerns in the CEE countries still are not on the top of the agenda of agricultural transition and rural development policy.

MULTIFUNCTIONALITY AND NEW ENTREPRENEURSHIP

As discussed so far, current EU rural development policy was set out in the agricultural dossier of *Agenda 2000*, which foresaw a considerably enlarged role for it in a reformed CAP as its 'second pillar'. These reforms also introduced the possibility for member states to increase funding for the 'second pillar' by shifting funds from the CAP's common market organisations (modulation), and gave member states discretion to include environmental conditions in agricultural commodity regimes (environmental conditionality). In the intention of the EU Agriculture Council, the impact of these 'second pillar' measures and the changes in the CAP should be mutually reinforcing. As a result, many subnational authorities and national governments have introduced measures to encourage and foster a 'multifunctional' agriculture based on environmentally sensitive farming practices and the need for rural development. The result in many EU member states, as well as in the local context, is a wide range of policy instruments with multifunctional goals and objectives, often originating at different geographic levels.

Multifunctionality is therefore the major new keyword of the recent EU agricultural and rural development policy and is expected to become even more the reference point of any next reform steps at any geographical level in the European context. The term "multifunctionality" is often linked to "rural development" referring to a new concept of agriculture not only considered as a narrow commodity branch, but a system of activities embedded in the local society and economy (Arzeni, 2001). In this context, agricultural activities are not only connected with the land and the production of food, but also with the management of the environment and the provision of services for the local community and the whole society. This is not an innovative concept in its literal meaning, because agriculture has usually played this role, but now the context has changed significantly. In fact, there is a wide debate about the new tasks that farms should carry out for society and the need for paying this work. Otherwise, on the one hand many social benefits will probably be lost, on the other hand funds currently spent for the CAP will be shifted in other directions.

Table 3: Main “weaknesses” of agriculture according to SAPARD proposals

	<u>Farm structure</u>		Access to credit	Farm technology	Land market	Access to markets
	Farms	Land ownership				
Bulgaria	Small size			Low mechanisation		Lack of well-organised market chains
Czech Rep.		Fragmented	Low liquidity, high indebtedness of farms	Insufficiently modernised	Barriers	Low co-operation
Estonia			Poor	Outdated technology, low investment	Slow reform, ownership unclear	
Hungary	Many small-holders, scattered plots		Poor	Obsolete equipment	Long term land lease system not adopted	No farm associations
Latvia	Fragmented		Difficult	Outdated machinery	Legislation lacking	
Lithuania	Fragmented			Lack of investment	Not functioning optimally	
Poland	Poor		Poor	Lack of modernisation		Poor
Romania	Fragmented		Poor	Poor	No market	Low
Slovakia		Fragmented		Lack of innovations	Insufficiently developed	Insufficient infrastructure, low co-operation
Slovenia	Scattered plots		Expensive loans	Low investment	Uncertain property rights	Poor horizontal integration on supply side
Frequency	7	2	7	10	8	7

	Available services and assistance	Farming skills	Quality of products	Subsistence farming	Hidden unemployment	Labour productivity	Yields
Bulgaria		Lack of modern skills	Poor	Important			Low
Czech Rep.			Insufficient		Important		
Estonia	Lack		Poor				
Hungary	Underdeveloped	Inappropriate					
Latvia				Important		Low	
Lithuania			Poor				Low
Poland	Poor						
Romania	No access to inputs			Important		Low	Low
Slovakia							
Slovenia		Inadequate			Under-utilised labour		
Frequency	4	3	4	3	2	2	3

Source: SAPARD proposals; Swinnen *et al.*, 2001

A “working definition” of multifunctionality

The term “multifunctionality” has been used with various meanings in the agricultural policy debate, depending on the country and on the context in which it has arisen. Developing a precise definition of multifunctionality may be an hard task; it is nevertheless necessary, and probably easier, to adopt a “working definition”. In this respect, the key elements of multifunctionality can be defined as follows (OECD, 2001):

- the existence of multiple commodity and non-commodity outputs that are jointly produced by agriculture;
- the fact that some of the non-commodity outputs exhibit the characteristics of externalities or public goods with the result that markets for these goods do not exist or function poorly.

Producing multiple inter-connected outputs can acquire economic relevance if this characteristic influences the way in which scarce resources are used in the economy to meet the demands of society. Moreover, the multifunctional characteristic can become relevant for policy if, among the multiple outputs generated, some are welfare-enhancing or welfare-reducing but for which no private markets exist. If, in such a case, a policy action is considered necessary to internalise an externality, the characteristics of the activity involved have implications for the design and the implementation of the correcting action.

There are essentially two approaches to the analysis of multifunctionality. One is to interpret multifunctionality as a characteristic of an economic activity. The particular characteristic that makes an economic activity multifunctional are its multiple, interconnected outputs or effects. These outputs can be positive or negative, intended or unintended, complementary or conflicting, reinforcing or offsetting. Some of the outputs are valued in existing markets, whereas others may elude the market mechanism. Multifunctionality, interpreted in this way, is not specific to agriculture; it is a property of many economic activities. This view can be termed the “positive” concept of multifunctionality (OECD, 2001).

The second way of interpreting multifunctionality is in terms of multiple roles assigned to agriculture. In this view, agriculture as an activity is entrusted with fulfilling certain functions in society. Consequently, multifunctionality is not merely a characteristic of the production process, it takes on a value in itself. Maintaining a multifunctional activity or making an activity “more” multifunctional, can thus become a policy objective. This view can be termed the “normative” concept of multifunctionality and this is under consideration here.

The rural firm and the new entrepreneurship

In Western Europe, many enterprises have emerged during the past few years, starting from an agricultural character by introducing new activities; many of them are linked with tradition but others are innovative and original. This is the multifunctional evolution of agriculture that is a spontaneous process generated by the difficulty of farms located in rural areas to achieve economic effectiveness and competitiveness. But this is also an answer to a particular demand by the consumer and the society for products and services these enterprises can properly supply. In this context, the concept of “farm” can be extended to include new activities in the firm organisation by using a surplus labour force. We can name this multifunctional organization as “rural enterprise” because it summarizes the principles of a rural development policy, that is the capacity of farms to integrate and to include extra-agricultural and profitable activities (Arzeni, 2001). The rural enterprise can be located not only in rural areas but also close to densely populated districts (urban areas), where there is a potential demand for agricultural products as well as for leisure and free time activities which many farmers have already begun exploiting.

There are many real examples of rural enterprises, which demonstrate how the multifunctionality of agriculture can actually work. We can classify these cases into four groups (Arzeni, 2001):

- *leisure, accommodation and free time activities*: in this category we immediately refer to agro-tourism that is actually one of the most common and well-known forms of multifunctional farms, because it combines agricultural production with the provision of catering and accommodation. But we can also include other activities linked to local crafts, made with agricultural products;
- *education, training and cultural activities*: there are currently many educational farms which help children to have a direct knowledge of domestic animals, food production and natural cycles. Moreover, cultural activities can find practical integration with agriculture as it is the case of farmers managing small museums, or musical and painting workshops;
- *health, fitness and therapeutic activities*: many farms that are positioned in this particular market have partially changed their structure into centres for rehabilitation (e.g. horse-therapy) or to take care of victims of social problems (e.g. former drug addicts). These entrepreneurial cases are more often located closer to the densely populated areas because there, the health-care demand is higher;
- *landscape preservation and environmental maintenance*: these are activities where public support is necessary because they are strictly non-market services. Some examples could be proposed about the maintenance of wooded areas or natural disaster prevention.

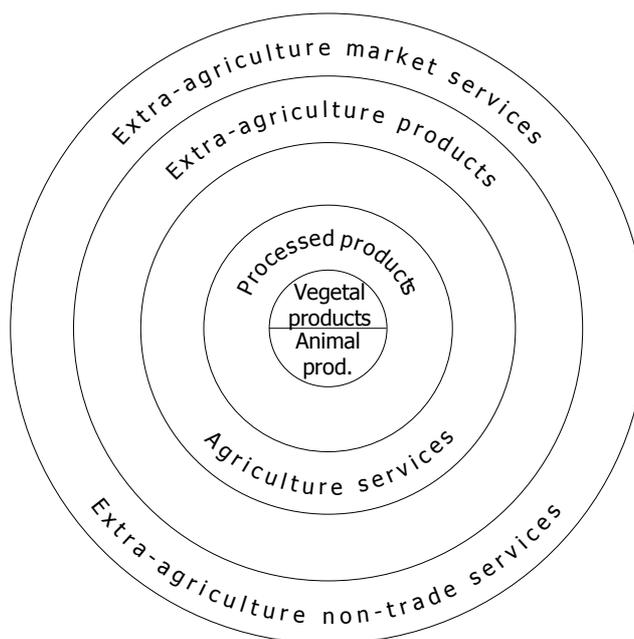
From these few examples we can argue how the concept of multifunctionality in agriculture could be translated in many different ways. Actually, every farm is multifunctional because it usually carries out activities that are not only limited to vegetable or animal production (e.g. the hiring of agricultural machinery). For this reason it is better to specify the definition with the aim of adjusting and fine-tuning it according to the new European policy guidelines. So we can say that a multifunctional farm should be characterized by:

- the core business of agricultural activities that is animal and vegetable production;
- one or more extra-agricultural processes or services that could be independent from agriculture but that the farmer itself integrates in the organisation of production.

We can introduce an example to make this argument more clear. The organic farm cannot be considered multifunctional “as it is” even if it provides many environmental non-market benefits for society. It becomes multifunctional when it extends the range of activities to include, for example, the retail shop management to sell farm and local craft products or illustrative material of the area. Hence, the concept of multifunctionality is strictly connected to the presence of agricultural and extra-agricultural activities in the same enterprise system, therefore sharing the same farm resources (figure 5) (Arzeni, 2001). In this sense the multifunctionality represents much more than an income opportunity. It is a new organizational form of enterprise combining agricultural production (the core business), with other activities. It is a “complete” enterprise which needs a high level of entrepreneurial skills.

All this can succeed if it is possible to train farmers in specific entrepreneurial skills not only for managing and producing agricultural commodities but also for taking part in the existing relationship network or to make new connections. These skills are not easily found in rural entrepreneurs, especially among old farmers, who mistrust every innovation not strictly linked with agriculture and intercompany dealings. On the contrary young farmers will have to assess whether the farm can be profitable with only the agricultural production or if it is necessary to widen the entrepreneurial range of services supply. These are personal choices that can not be supported without considering many factors such as farm localization, land size, resource availability, etc. Present rural development policy in the EU as well as in any member state needs an intensive effort for training and supporting entrepreneurship because the rural enterprise, as described, requires an entrepreneur able to produce, manage, promote and sell different products and services. Education and training should be organised to achieve this professional profile using a balanced mixture of technical and human relationship skills. The role of extension services is very important to achieve this improvement but they must adjust their range of advices by including extra-agricultural services and by strengthening the socio-economic network on which rural development is based.

Figure 3: The multifunctional enterprise: a synthetic diagram



Source: Arzeni, 2001

CONCLUDING REMARKS

The gradual change of direction of the EU agricultural policy represents an historic opportunity for the Central and Eastern European countries in the perspective of their accession. They can re-design their transition reform and policy making their own agriculture adjust in concordance with the new EU strategies. As shown, this new strategy mainly implies redefining the role of agriculture in the light of a sustainable and integrated rural development. The main constraints and issues of agriculture and rural areas in transition can therefore dealt with the new concepts and instruments, as well as funds, provided by the European Union.

This has to be a major objective of agricultural and rural development policy in the CEECs. However, a detailed analysis of the main issues also suggests some relevant policy implications for this gradual acquisition of the EU concepts and tools. First, a differentiated (among countries and regions) approach is needed for a successful rural development strategy in transition countries; this implies that policies have to

be managed and implemented at a marked decentralised level. Second, rural development policies have to be complementary with sound and appropriate macro-economic policies and structural reforms. Third, policies directly aimed to improve capacity and institutional building are also crucial. In this respect, it clearly emerges that investments in education and skills would contribute to several objectives: improvement of productivity, creation of new enterprises, quicker adjustment to the market economy. Moreover, institutional innovations are very often the key-solution to market imperfections and imperfect property rights which strongly constraint the access to credit and finance. Finally, no institutional improvement can be steadily developed if low incomes in rural areas remain a crucial constraint to structural adjustment; in this respect, policies for poverty alleviation are still needed.

Under this general framework is now possible to introduce the specific issues of the areas under study (the Croatian counties of Zadar and of Šibenik-Knin). These areas are called "*areas of the special government concern*" since they have been directly struck during the Croatian War of Independence. According to the critical economic, demographic and social situation of the area, finding appropriate measures and activities to turn the negative development courses into the positive direction can be assumed as the priority task for a development strategy plan for these area. Agriculture as well as a sustainable recovery of the whole rural economies are, in this sense, key- issues. It follows the need for an organised and efficient development management in the area with particular attention to the main agricultural potentials. The renewed EU vision and instruments on rural development can become the appropriate means to develop these potentials.

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