

Summary

The rural development programme is the second pillar of the Common Agricultural Policy (CAP). The programme consists of a large number of measures designed to promote economic, social and environmentally sustainable development of rural areas. When the current seven-year programme ends in 2013, it will have cost a total of SEK 36 billion, half of which has come from the national budget. Based on the evaluations of the rural development programme measures, this report aims at answering the question of what society receives in return for these funds and propose revisions for the new programme period (2014–2020).

Background

Rural areas differ from urban areas in several respects. Compared with urban areas, the levels of population growth, demographics, employment, incomes, education and service are less good in rural areas. The increasing concentration of economic activities in Swedish urban areas over time is due to the advantages of economies of agglomeration, i.e. costs become lower when similar activities are located in the same place. The lack of economies of agglomeration in rural areas is not a market failure in itself, but the relocation of businesses and people to larger towns and cities creates negative consequences for those that remain in rural areas.

Nutrient leaching and the emission of greenhouse gases are agriculture's most important negative environmental impacts (negative externalities). In a historical perspective, agriculture has contributed to increased biological diversity – a public good – by maintaining an open and diverse landscape. However, these positive contributions have decreased as a result of changes in land use and the loss of certain types of farming landscapes, primarily in

intensively farmed areas. Just over half of all threatened species in Sweden are found in agricultural landscapes.

The basic idea behind the rural development programme is that the rural development, left to its own devices, is not satisfactory. It is therefore important to analyse how well the programme's measures are meeting the economic and social challenges of rural areas and the agriculture's most important environmental problems. The focus is on the existence of market failures such as external effects, public goods, high transaction costs or information problems. This analysis is based on the principle that agriculture should be treated in the same way as other sectors in the economy.

To identify the effects of the programme, it is insufficient to merely *follow up* the measures, rather a *contrafactual analysis* is required to establish what has occurred because of the measures. However, a lack of access to data has meant that it has not been possible to objectively evaluate the large number of the measures, which makes the results uncertain.

Measures and effects of the Swedish rural development programme

The rural development programme is decided at national level based on a menu of measures determined at EU level. These can be divided into five main groups: support to the rural economy; enabling support; support to quality of life and cooperation; support for the preservation of biological diversity; and measures against nutrient leaching.

Support to the *rural economy*, i.e. farming, food processing and diversification, is dominated by large capital subsidies. A significant portion (27 per cent) of the investment costs of these activities are paid by society. This mostly concerns support for the production of goods lacking significant external effects. There is strong evidence that these subsidies displace normal activities (up to 90 per cent), in particular with regard to support to investments in agriculture and in processing. In conclusion, support in this category has been income redistributive to a very large degree, rather than efficiency boosting.

With regard to *enabling support*, i.e. skills development support, training and information support, infrastructure support and support to cooperation/innovations, these could in theory result in

efficiency increases. But in practice, whether these forms of support have a positive effect depends on how they are designed and implemented. Support to innovations has not resulted in new products, but has primarily gone towards marketing. For most of the training initiatives analysed, no positive effects have been shown. In general, one could say that the courses have been too short to have any noticeable or lasting effect.

Support aimed at improving *quality of life and cooperation* includes, among other things, initiatives in the daily consumer goods trade, the improvement of premises, information and conferences about rural development. These forms of support are very unlikely to displace normal activities, but nothing is known about their long-term effects. The theoretical underpinning of the measures (the build-up of social capital) is weak, since nothing suggests that it is a lack of social capital that is holding back development in Swedish rural areas. Furthermore, it is doubtful whether the initiatives should be implemented in project form of temporary character since the problems have a more permanent nature.

The environmental support is dominated by four forms of support that are primarily motivated by the *preservation of biological diversity*: support to disadvantaged areas; support for the cultivation of grassland in northern Sweden, support to pastureland and support for organic cultivation. Together these account for three quarters of the environmental budget and more than half of the entire programme budget. But the support payments have not succeeded in stopping the deterioration of biological diversity according to the Swedish Species Information Centre. However, model estimates show that the removal of certain forms of environmental support, in particular the support to pastureland, would negatively affect biological diversity further. Therefore, to a certain extent, the environmental support may have helped to preserve biological diversity in Sweden.

Agriculture's negative externalities are overwhelmingly managed using selective measures aimed at capturing nutrient surpluses or the prevention of their leaching. Compensation is offered for growing of catch crops and/or spring land preparation and for creating riparian boundary strips and wetlands. Both field measurements and model estimates suggest that the support has reduced nutrient leaching. However, the placement of wetlands and riparian boundary strips in the landscape is critical to their

effectiveness. Looking at the composition of the programme in its entirety, it is clear that *in principle* it is a correct prioritisation that the programme is dominated by environmental measures. Market failure primarily exists with regard to the production of public goods associated with the agricultural landscape, which gives rise to the use of sector-specific measures. However, looking at the *practical design* of the environmental measures, the balance between broad-based environmental support and targeted support is incorrect. Too many resources are invested in broad-based forms of support that have doubtful environmental effects. In certain cases, they function mainly as a form of income support.

Proposed improvements for 2013-2020

The Swedish rural development programme has remained essentially unchanged since Sweden joined the EU, but based on the evaluations that have been carried out there are grounds to reform the programme. The doubtful utility to society and the unclear effects on the central goals (increasing the agriculture's competitiveness, preservation of biological biodiversity and rural population growth) both speak in favour of reformation. Many of the programme's measures mainly function as a form of income transfer. However, to achieve income equalisation, social policy is more efficient. The programme should therefore be targeted at increasing efficiency in resource allocation and avoiding forms of support that are likely to displace normal activities. In practice, this means that support to private goods in functioning markets should be avoided. Rather, support should be directed at goods that the market fails to provide. When the market does not function well, for example, because of high transaction costs or information problems it is generally better to try to remove or alleviate the underlying problem than compensate for its damaging effects.

In the current programme, the emphasis is on agriculture, agriculture-related activities and capital subsidies. One problem is that there are too few agricultural businesses to maintain a thriving countryside. Rather, to develop rural areas the entire rural economy should be the focus. This means investing in measures that create better conditions for all businesses rather than subsidising the capital of certain agricultural businesses. Subsidising activities that have positive external effects is justified,

but it is important that the subsidy is on par with the value of the external effect.

Support to the rural economy should, to a greater extent than today, compensate for the disadvantages of sparsely populated areas through the provision of advice, training and specialised services. Furthermore, innovative activities should be supported since the market tends to generate too few innovations. Innovation support should be coordinated with support for innovations in other sectors.

In all likelihood, the rural development programme cannot influence the economic and social situation in rural areas more than marginally. Rather than trying to reverse the population flows, the focus should be placed on measures that alleviate the problems associated with depopulation. It therefore seems reasonable to focus on a few essential measures, such as access to basic services, rather than a wild variety of projects. Initiatives in the form of permanent structures should be prioritised instead of those in project form.

The programme should be revised so that more environmental benefits are generated in relation to the investment. This should primarily take place through the redistribution of funds from broad-based support, such as grassland support, and support to entire growing systems, such as organic cultivation, to selective measures. Support should not be paid “in the name of fairness” if the environmental benefit is low. New policy instruments should be introduced to the programme, mainly with regard to the design of measures at county level. Furthermore, the state should adopt a more proactive role by procuring environmental services when necessary. Basing payment on achieved environmental results should also be tested.

Knowledge about the programme’s effects is inadequate and uncertain and it is unreasonable for society to invest major sums of money without making sure it is used wisely. The funds granted for the analysis and evaluation of the programme’s effects are very small in relation to the programme’s total funds and need to increase. The evaluation of the rural development programme should be conducted by an organisation that is not in a position of dependency on the agency or agencies designing the policy.