Private Initiatives for Rural Development: Ideological Cop Out or Engine for Progress

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Research Report No. 3

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Acknowledgements

This discussion paper was delivered at a symposium sponsored by the Congressional Research Service and Joint Economic Committee, U. S. Congress, September 1988. The symposium's title is "Toward Rural Development Policy for the 1990s: Enhancing Income and Employment Opportunities." Emilio Pagoulatos and Gary Johnson provided useful comments. Dorine Nagy typed this report. Responsibility for content, including errors rest with the author.

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Abstract

This report identifies a research and policy agenda that can contribute to rural development and antipoverty initiatives during the 1990s. It integrates a discussion of private initiatives for rural development into a broader discussion of the issues. Two theories of underdevelopment and poverty, one motivational and the other structural, serve as a basis for defining quite different research and policy agendas. To provide some closure on these divergent approaches it is argued herein that economists must more rigorously examine the philosophical and political economic foundations of their theories. One reason this is needed is that recent contributions to the theory of public choice rehabilitate the classical economic argument for minimal state action.

An effective and efficient rural development policy, moreover, must analyze the distribution system that delivers goods and services to rural communities. There is evidence that noncompetitive distribution channels distort prices in some rural communities and transfer wealth from them. In addition, many rural communities are at the end of distribution channels. Therefore, even in competitively structured channels, the relatively high costs of delivered goods and services for productive activity and consumption retard economic development and standards of living. Changes in the structure of rural households and the employment shift out of agriculture limit the ability of rural families to offset these higher costs via traditional household production activities.

Cooperatives of many types–agricultural, rural electric and telephone, wholesale grocery, and consumer cooperatives–have been a major component in market-oriented public policies to promote effective distribution of goods and services to rural America. More recent institutional innovations that enhance private initiatives are public venture capital funds and nonprofit agencies. Research on rural distribution channels and the appropriate mix of private and public initiatives should be a major component of any new rural development policy.

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> "Yeobright loved his kind. He had a conviction that the want of most men was knowledge of a sort which brings wisdom rather than affluence. He wished to raise the class at the expense of individuals rather than individuals at the expense of the class. (Thomas Hardy, Return of the Native, p. 194)

As a discussant at this symposium on Rural Development I have been asked to comment on presentations by Phil Burgess, Peter Fisher and Douglas Shumavon (Russo and Shumavon) and to discuss cooperatives as a vehicle for rural development. I would like to do this in the context of a discussion of two fundamentally different theories of poverty and the role of private institutions in the development process.

After listening to these presentations, and others in the symposium, a general observation comes to mind. We probably have not cast our nets widely enough to have the intended impacts that this group wants to have. Admittedly, we have marshaled several facts that document the extent of rural underdevelopment and the efficacy of certain approaches for alleviating the problem; but, I don't think that we will convince our critics of the necessity of work in this area by presenting such facts. If, indeed, that were the case, we would have more rural development and less rural poverty than we have today.

What is the nature of the problem in rural development, and the related core issue–rural poverty? What is the critical impediment? I would suggest that there are two competing ideas as to what the nature of the problem is and what the major impediment is. One idea is that the problem is fundamentally motivational in nature. The other is that the problem is fundamentally structural in nature.

Taking motivation first, in the last eight to ten years we have seen resurgence of the classical economic concept that the sources of underdevelopment and poverty are indeed motivational. What the government needs to do is provide hope for people, possibly get off their backs, possibly revitalize the private sector, and possibly instill self-reliance in people that have forgotten the meaning of the term.

With regard to self-reliance, some proponents of motivation have advanced the notion that a dollar earned is worth several dollars in transfer payments. In other words an earned dollar has more utility to a poor person than several dollars in transfer payments. Perhaps "Yeobright's wisdom" or pride is involved. But if a child is hungry and a poor parent has only one dollar to feed him as opposed to ten or whatever, maybe it's not true.

Also, after having listened to Phil Burgess, there is the notion of the motivation of the rich in society. As a graduate student working under Lee Bawden in the early 1970s, one of the first papers I read was

Hochman and Rodgers neoclassical analysis of transfer payments (Hochman and Rodgers, 1969; 1970). Their intent was to provide a theoretical basis for government transfer payments, however their effort provided impetus to the nascent public choice school of Buchanan and Tullock. A fundamental proposition therein is that government failure may be worse than market failure (Wolfe). Public efforts to improve social welfare may, in fact, reduce it due to organizational inefficiencies, and disincentives. In other words, the voluntary sector can do just fine because the rich, if given the opportunity and encouragement to contribute to the poor, can do so in a socially optimal fashion. Altruism as well as profit maximization can energize private initiatives to benefit the poor. This is a sophisticated generalization of classical political economy with its minimal state presence.

The second theory of poverty and underdevelopment is structural. Structure is something that we have all talked about today, the idea of physical and human resource constraints, the idea of prices being out of whack, the organization of economic activity –including nonprofit agencies, public venture capital firms, and cooperatives to fill gaps in performance left by investor owned firms. These are the bread-and-butter of the social scientists seated around the table today.

Well, one might ask what is the point of bringing up these two major competing theories of underdevelopment and poverty? I think that the two papers presented by Peter Fisher and by Douglas Shumavon (Russo and Shumavon) reflect professional jet lag in our thinking because the papers move to directly the use of public intervention to solve market failure problems. They instinctively move to how the government can put more money into the system, how the power of the state can be used to alter the opportunity set facing private decision makers, and how new institutions can be created by government so that more rural development occurs.

Yet, there is a more fundamental question, and there is a more fundamental contribution that we have to make to the political debate before this is going to happen. We have to answer the following question: how have market forces worked? Frankly, I think it is a wonderful time to do that. As a matter of fact, the research presented by Swanson (Skees and Swanson) today provides answers. We just need to back up a bit, ask the question, and get it out into the political arena and debate.

Market forces have not worked to enhance rural development and reduce rural poverty during the 1980s. But even if we provide that answer, we probably are not going to answer our critics, because antecedent to our analysis of the market are assumptions about things like entrepreneurial zeal, and values that promote self-reliance. Much of the recent criticism of work on poverty argues that these are endogenous. It appears that we need to answer questions such as, has there been an expansion of entrepreneurial zeal, and has there been a shift in the values of the leadership of American corporations over that last eight years with regard to rural poverty? I think what we are talking about here is

a test of Phil Burgess' hypothesis: Have large American corporations over the last eight years energized and motivated themselves? If so are they acting on the basis of altruism or profit maximization? Are they promoting rural development?

As Phil says, they are to a certain degree. Is the amount of the response commensurate with the need? Do they need assistance, as he suggests, because sometimes they're like bulls in china shops when they get into this activity?

We also need to ask has there been an increase in self-reliance among the rural poor and has there been a shift in their valuation of it? Do they value a dollar earned through the market more than several dollars of transfer payments even when their child is starving? Put it right in its most stark hypothetical form and answer the question.

My fundamental point is that the center of the intellectual arena on the issue of rural poverty has shifted away from the technical expertise located in this room. We need to look more carefully at the philosophical and political economic foundations of our economic analysis. I say this after having read a number of pieces ranging from the Robert Nozick's, *Anarchy, State, and Utopia*, a libertarian treatise, to David Levine's, *Needs, Rights, and the Market*, a neo-Ricardian approach to the issue of rights and allocation of resources and poverty. Philosophers are introducing economics into philosophical analyses of distributive justice. What distribution of income is right? We are implying that the current distribution in rural America is wrong. I am not so sure everyone would agree. As Nozick concludes:

> "The framework for utopia that we have described is equivalent to the minimal state... The minimal state treats us as inviolate individuals, who may not be used in certain ways by others as means or tools or instruments or resources; it treats us as persons having individual rights with the dignity this constitutes. Treating us with respect by respecting our rights, it allows us, individually or with whom we choose, to choose our life and to realize our ends and our conception of ourselves, insofar as we can, aided by the voluntary cooperation of other individuals possessing the same dignity. How dare any state or group of individuals do more. Or Less" (p. 333-334).

This minimal state is formally equivalent, Nozick argues, to a competitive market economy with no government intervention.

Let us shift now to structural analysis. The work that Peter Fisher has done is good. I commend it, and think his paper is definitely worth reading because it is a very careful explanation of how markets can fail and of why more economic activity is not located in rural America. He, moreover, does us a great service by carefully documenting some of the pitfalls of looking at things quickly.

In his analysis of the Deere & Company spinoff, Fisher basically argues that it is a way to bust a union and shift work to lower-priced sites. Some critics, however, might suggest that a new economic institution is in place; and although they are reliant on Deere, they could probably shift to production of some other component part for another company, possibly even a foreign firm. In other words, this new institution may find opportunities for rural workers that would otherwise be missed. I tend to think, however, that if one empirically investigated the performance of spin-off firms Peter's analysis would carry the day. Certainly, the evidence on worker buyouts of rural based enterprises such as Rath Packing suggest little long-term benefits.

Most rural development analysts have focused on expanding production to produce jobs, and to produce incomes. They ignore or downplay the study of distribution of goods and services in rural areas. Peter falls into this trap a little bit in his paper when he makes the statement that making changes in the distribution of services in a rural area will not increase the welfare of rural residents.

I would like to take this oversight to task. Rural residents, according to the dependency hypothesis that Professor Brown put forward and Peter mentioned, can be exploited not only by the operation of noncompetitive rural labor markets but also by the importation of goods and services. Monopolies or noncompetitive distribution systems can extract income from an area. The delivered prices that rural entrepreneurs must pay for inputs imported to the area for productive activity, and the prices that rural residents must pay for consumption goods are crucial parameters for any rural development initiative. Permit me to give you an example.

Working for the Attorney General of Vermont on the grocery industry in Vermont in the early 1980s, we found that two national chains dominate the Vermont retail grocery market (Cotterill, 1986). They sell approximately 60 percent of the supermarket groceries in Vermont. One of those chains gave us their profits before they realized what they had done, I think, because the profit-sales ratio on this chain was in excess of five percent of sales, whereas the industry profit rate throughout the country is about 1.5 percent of sales. This chain made 3.7 percent of its sales in the State of Vermont and 15.1 percent of its corporate profits came from those sales. Moreover, this was not a small regional chain. It is one of the top 15 chains in the United States, controlled at that time by one of the worlds pre-eminent corporate raiders, Sir James Goldsmith. This is an example of the dependency hypothesis. The food distribution system is organized noncompetitively and resources are being taken out of the area.

One might counter, "Well, maybe they're reinvesting some of these earnings in new plant and equipment in Vermont." In fact the two leading chains suggested that they would do that when this came to light. I talked with the Assistant Attorney General about a year ago and he said that they talked about it for a couple of years however they have made only marginal changes in their operations.

I mention the above example for another purpose as well. A second major point is that contrary to myth, I would hypothesize that it is more expensive to live in rural areas with regards to food procurement than it is to live in an urban area. Why can't rural consumers "grow their own?" First, most of rural families now are nonfarm. Second, most husband-wife households have two workers in the family. The wife is not at home. That means that there is significantly less time for household production in rural areas that, according to tradition, is supposed to save money. Moreover even if there is household production, the cost of inputs to make, for example, jam–sugar, jars and so on and so forth–may very well be equal to or more than the cost of the purchased product. Home production may not return enough to add to household utility.

Well, what are the implications of this? It is important because as Bonnen explained this morning, the definition of poverty is based to a significant degree upon the cost of food. Food Stamp benefits are also based upon uniform assumptions about the cost of food. Rural America is again disadvantaged relative to urban America by these computational formulas because if this hypothesis holds for most of rural America as it does for Vermont, the cost of food is higher in rural areas, not lower.

One can expand this analysis. As a matter of fact, I would hypothesize that it is more expensive with regard to most goods and services to live in rural areas rather than urban areas. The lack of competitive distribution channels is important in many communities; however, there may be an even more pervasive and fundamental problem. Dunne, for example, argues that the delivery of quality education programs to rural children costs more because there are fewer children, higher transport costs, and other costs of isolation, not the least of which is the difficulty attracting top flight teachers (Dunne, p. 55). Rather than being at the source of the distribution channel and being able to access finished goods and services more cheaply than urban consumers, rural consumers increasingly find themselves at the end of a distribution channel that flows from urban areas, or foreign countries via urban areas to rural communities. Rural consumers are at the end of the line. Thus goods and services of like grade and quality, if available at all, cost more even when distributive channels are organized competitively.

Clearly market-based strategies for rural development, can be an important component in an overall rural development plan. The idea of voluntary efforts by the private sector, the civic leadership coalition, the pre-1929 classical approach that Phil mentioned can be effective, but I am enough of a Keynesian and a modernist to think that it's not totally adequate. The mixed economy is here to stay. We also need joint public/private initiatives. Fisher's idea of publicly provided venture capital is intriguing. Shumavon's (Russo and Shumavon) analysis of the role of nonprofit agencies is helpful.

Cooperatives, private businesses owned and controlled by users rather than investors, also have a role to play. Agricultural cooperatives, rural elective cooperatives as evidenced by Bob Bergland's activities, and other rural based cooperatives are extremely interested in these questions. Throughout most of this century cooperatives have played a major role in promoting efficient distribution of productive inputs to rural America. They also have provided farmers with some control over the marketing of their products, created more efficient marketing channels, and increased the prices farmers receive. Given the current wave of mergers throughout the food system, however, even the largest agricultural cooperatives are small when compared to leading firms of the sector.

During the remainder of this century rural based cooperatives face critical strategic questions concerning generation of investment capital, organization, and focus (Cotterill, 1987). For cooperatives to strengthen their role in the development of rural America, there needs to be continued public support for cooperatives via economic research, extension education, and public policies conducive to the organizational and operation of user owned and controlled businesses (ACS).

As this last comment indicates, public policy has a role to play facilitating and channeling private initiatives. There is a need for setting the rules of the game. There is a need for information. Regional planning, which Peter is a professor of, is one approach. Another area that needs to be emphasized but hasn't been mentioned today is regulation. At the federal level, the U. S. Congress and agencies like the Federal Trade Commission, the Interstate Commerce Commission, and the Department of Agriculture set policies that very often structure the terms of trade between rural and urban areas. If we are to promote equal opportunity for rural Americans, we need to look at the impact of these policies on rural development.

My concluding observation is that there is no systematic and coordinated research agenda on rural distribution channels, the appropriate mix of institutions and the interaction of private and public efforts to foster rural development. The work presented in this symposium is a very modest beginning. It is hard to envision an effective and efficient rural development policy that would not make the study of these issues a top priority.

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