Rural Development Strategy

Eastern Europe and Central Asia

Csaba Csaki
Laura Tuck
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(List continues on the inside back cover)
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The World Bank
Washington, D.C.
Tables

Table 1. The Significance of Rural Populations in ECA .................................................. 12
Table 2. National and Rural Poverty Indicators for ECA ................................................. 13
Table 3. Status of Agricultural Reforms in CEE and CIS Countries in March 2000...... 18
Table 4. Priority Actions for Rural Development in the Region .................................... 43
Table 5. Priority Projects for Rural Development in the Region ..................................... 43
EXECUTIVE SUMMARY

This paper summarizes the World Bank assistance strategy for rural development in the ECA region. The rural sector includes the people; economic development activities; institutional, economic, and social infrastructure; and natural resources in rural areas and is thus not confined to agriculture. This paper focuses on Bank activities that support rural development and policy reforms designed to improve rural well-being and increase the competitiveness of farms and rural businesses. Natural resources and social and institutional development issues are addressed separately.

Our strategy lies within the overriding regional objectives of poverty reduction and economic growth, improved public sector management, an expanded role for civil society, support for development of a market economy, and environmentally sustainable development. In rural areas we plan to assist our clients in two principal areas:

- Resumption of agricultural growth; and
- Rural development outside the agricultural sector.

To do this, we will emphasize approaches that:

- Focus on reducing rural poverty; and
- Are community driven.

Following an overview of the sector and developments since the transition, each of these areas and approaches are described in more detail.

Agriculture, the Rural Economy, and the Status of Transition

Agricultural Production

The transition region has a substantial part of the world’s agricultural resources (figure 1). In the mid-1990s, the countries of the region comprised 13 percent of the world’s area suitable for agricultural production and 19 percent of arable land.1 The region makes a substantial contribution to world output in practically all of the main agricultural products. On average, this contribution is around 10 percent.

The share of agriculture in employment and national income in ECA countries is far greater than the average for Western developed countries. In 1997–98 the agrarian sector contributed about 9 percent of the GDP for the transition region as a whole, while the proportion

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1 1996 number.
of the agricultural population was 16 percent. However, there are very substantial deviations from country to country in regard to this sectoral role. The share of agriculture in the GDP is only 5 percent in the EU accession candidate countries, compared to 31 percent in the Caucasus and 24 percent in Central Asia. The contribution of agriculture to the GDP is much lower than the role it plays in employment. This is an indication of the low productivity of agriculture and low levels of efficiency that are below the developed country average.

The region has great geographic and climatic diversity, and the pattern of agricultural production is similarly diverse. Agricultural production has declined dramatically since 1990 in all countries of the region except Turkey. Between 1990 and 1996 it fell by an average of 7.8 percent per year. The decline was due to a number of factors, including initial confusion surrounding the transition; declines in consumer demand (especially for more expensive livestock products) following reduction of food subsidies and deterioration of economic conditions; the collapse of traditional market systems, export markets, and the internal “Eastern Bloc” trading system; declining input use; and deteriorating irrigation infrastructure and machinery stock associated with the collapse of the cash economy in several countries. Output has now stabilized at about 70 percent of pretransition levels in Central Europe, but is still declining in some CIS countries. (See tables 1 and 2.)

**Rural Poverty**

There has been a sharp rise in national poverty and inequality in ECA countries since the beginning of the transition. National poverty incidence has reached very high percentages in many countries, according to recent World Bank poverty assessments (figure 3). Rural poverty has increased in line with the rise in national poverty, if not more so. Within 15 of the 20 ECA countries for which poverty data are available, the incidence of poverty in rural areas is as high as or higher than in urban areas. On average, over all countries, rural poverty incidence is 60 percent higher than urban incidence. Because urban populations tend to be larger than rural populations, the contribution of rural areas to the total number of poor is less. Even so, in 10 of 20 countries, the rural poor account for as much as or more of the total poor than do the urban poor.

Some other subregional patterns in rural poverty are worth mentioning. The Central Asian countries (the Kyrgyz Republic, Tajikistan, and Kazakhstan) comprise one ECA subregion in which rural poverty appears to dominate the poverty profile. Central and Eastern European countries show a mixed pattern, with some countries exhibiting a very high rural poverty contribution to the total poor (Poland, Romania, and Macedonia) and some very low (Slovenia and the Czech Republic).

**Access to Services and the Broader Rural Economy**

Since the beginning of the transition, there has been an overall deterioration of the rural nonagricultural situation throughout the CIS. The actual dismantling of large-scale farms and the

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2 Food and Agriculture Organization (FAO).
3 WDI.
4 World Bank, *Poverty Trends and Voices of the Poor.*
deteriorating financial conditions of the remaining ones have significantly reduced the resources available for social services and rural infrastructure (figure 4). In some places, responsibility for rural social services and infrastructure has been transferred to the municipalities, but the question of their financing is still mainly unresolved. As a result, rural social services remain seriously underfunded. An economically declining rural environment and nonresponsive governments have also significantly retarded the emergence of a private-based rural nonagricultural sector.

The situation in Central and Eastern Europe is considerably better than in the CIS. The initial state of rural nonagricultural conditions was significantly more developed and it has been much less affected during the reform years. In a number of Central European countries, such as Hungary, the Czech Republic, Poland (with the exception of some underdeveloped areas, such as southeastern Poland), and the Baltics, a visible recovery of rural nonagricultural activities can be observed. This recovery is driven by the private sector and local municipalities, which are gaining increased fiscal and legal autonomy. The resumption of overall growth in these countries and the decline in unemployment have made a positive impact on the rural sector, which is probably most visible in the emergence of flourishing private rural service sectors and the ability of the rural areas to improve their social services and infrastructure.

Agricultural Policy Reform and Recovery of Growth

Before the transition, agricultural and food production was largely centrally planned to maximize output, with limited consideration for efficiency. The large-scale livestock and crop cooperatives were unsuited to market-based private agriculture. Creating viable private farming based on private ownership of land and allowing market signals to determine levels and types of production have been some of the most difficult tasks of the transition period.

In 1990–91 the region set out on the path of creating market economies based on private property. In all countries the most important basic elements of the reform process have been:

- The liberalization of prices and markets and the creation of a market-conforming incentive system in the rural sector
- The privatization of land and transformation of the inherited farming structure
- The de-monopolization and privatization of food processing and the trade in agricultural produce and capital goods
- The creation of a functioning rural financial system and establishment of the institutional structure and system of state administration required by market economies.

Table 1 summarizes a Bank assessment of recent progress toward reform for individual countries. In general, the Central European and Baltic countries have made the most progress, while the core CIS countries and Turkmenistan and Uzbekistan have reformed the least. The prospect of accession to the European Union has facilitated the achievement of consensus concerning reforms. A number of lessons can be drawn from the experience to date:
• In general, the reform process has been slower and more difficult than expected, and has resulted in slower recovery of growth than expected. This is partly because economic transformation is so complex and also partly because the creation of genuinely private farms has been difficult in many of the CIS countries.

• Price and market liberalization has generally been easier than creation of private farms, rural finance, liberalization of agroprocessing and input supply, and institutional reform.

• It has been easier to implement reforms when the broader economic situation has been favorable.

• Development of the nonagricultural sector of the rural economy has been key to the recovery of agriculture, permitting creation of new employment opportunities in other sectors and reduced employment and greater efficiency in agriculture.

• The best progress has been in countries that have reformed radically and rapidly rather than gradually, despite short-term adjustment difficulties.

Reform in Central Europe has been politically easier (though complex enough) than in the CIS for many historical reasons. These Central European countries had a shorter experience with central planning and had relatively sophisticated economies and established middle classes at the start of the reform period. They did not experience the civil unrest that destroyed economies in the Balkans and the Caucasus, and were not dependent on subsidies from Russia, as were several Central Asian and Caucasus countries. The “transition shock” to institutions and the role of the state in society was thus less severe. In some CIS countries, particularly Russia, the trend toward decentralization in government, with a more complex pattern of relationships in political power, has posed particular challenges when reforms initiated at a federal level have been difficult to implement at regional or enterprise levels.

Existing World Bank Portfolio

The existing loan portfolio in ECA countries consists of 55 rural and natural resource projects, with a total of $2.2 billion in IBRD/IDA commitments. Out of the committed amount, $1.8 billion has been disbursed. One of the striking features of the rural development portfolio is the diversity of activities that fall within this rubric. There are probably more distinctly different types of activities carried out under the heading of rural development than under any other heading. These include, for example, agricultural sector adjustment loans; land titling, registration, and cadastre; farm privatization and restructuring; rural finance and microcredit; research and extension and rural advisory services; rural infrastructure; irrigation; drainage and dam safety; forestry; biodiversity; water resources; flood control; livestock and animal health; agro-industry and marketing; crop protection; and general rural development (including social services and infrastructure).

The nearly $2 billion that the World Bank has contributed to the rural development of ECA countries since the early 1990s is a relatively marginal amount when compared to the
overall inflow of foreign capital in the region. Since most of the foreign financing has gone to non-rural areas, however, it can safely be concluded that the Bank has been one of the main outside financiers of the rural sector in the region. The World Bank’s role and leverage, however, have been rather different in various parts of the region. Due to the slower pace of rural economic reform, the Bank’s financing, and therefore impact, has been rather modest in the larger CIS countries, especially Russia, Ukraine, and Belarus. In most of the “front-line” EU accession countries, such as the Czech Republic, Hungary, and Slovenia, the need for Bank financing has declined significantly, even as the countries continue to welcome the Bank’s policy advice. At the same time, the Bank’s projects provided significant financing in the faster-reforming countries in the Caucasus, Central Asia, and the Baltics, as well as in Bulgaria and Romania. Consequently, the Bank’s impact on policy developments in these countries has been more substantial.

Strategy for Assisting Rural Development

Broad Objectives

The region’s approach to rural development is evolving in line with the current Bank-wide approach. The traditional focus on agriculture has not been adequate to bring about significant reductions in rural poverty. Rural poverty and rural development need to be considered in a cross-sectoral context because of the “connectedness” of rural residents to many economic sectors, only one of which is agriculture. Viewing rural development more holistically has implications as to how ECA’s strategy should be structured and implemented.

The regional rural development agenda of the 1990s emphasized the transition to a market-based food and agricultural system, the need to develop an efficient private sector with appropriate public services, and the protection of natural resources. In the later stage of the transition, the importance of rural communities and rural livelihoods has also been recognized. Building on lessons of the past and insights from recent poverty assessments, the region’s rural development efforts in the future will focus more on people, particularly poor people, using “bottom-up” nonsectoral community participatory approaches. Rural people are not only farmers or agricultural workers. The Bank intends to widen the scope of rural development and to reduce poverty wherever it is found in rural areas. The Bank will do this in close collaboration with Bank colleagues in other sectors (such as infrastructure, social services, and finance), to ensure consistency with their approaches as the Bank encourages their expansion of work into rural areas.

The Bank’s evolving approach to rural development also will have to take into account two region-specific phenomena. One is the so-called “reform fatigue” of the core CIS countries, which is likely to require some adjustments in how the Bank addresses the reform agenda. Development of more innovative approaches to working with these countries will be a key focus in the coming year. The other phenomenon is the increasing diversity in the status of rural development among countries inside the region. While the Bank’s approaches have always been specific to the particular situation in individual countries, there will be more variation in the
portfolio over the coming years. The Bank’s strategy has evolved as a result of many of the
lessons it has learned from its past successes and failures.

Specific Objectives

- The Bank’s experience indicates that it can play a significant role in reducing rural
  poverty and in rehabilitating the rural sector throughout the region. The Bank’s
  role, however, will vary significantly from country to country and in various rural
  subsectors. Since the resources allocated to rural development will be significantly
  reduced over the coming years, the Bank will focus selectively on the areas where it
  has a comparative advantage, where it has working models, where it is likely to have
  the greatest impact on the ground, and where it can best support inclusive growth.

Components of Regional Strategy

In rural areas, the Bank’s strategy will support development in both traditional agricultural
activities and in off-farm rural activities.

Resumption of agricultural growth. The massive decline in agricultural GDP between
1990-1996 means that the first priority for the region must be agricultural growth. Of course
some of this contraction was appropriate as many non-economic activities were closed down.
Nonetheless, there is tremendous scope to increase economically viable agricultural production
in the region. To achieve this, the Bank will continue to stress rapid policy change, increased
private land ownership, complete privatization of agro-processing and marketing, support of
 technological change in agriculture, and stimulation of nonfarm employment.

Expanding nonagricultural rural development. In the forthcoming period, the Bank
intends to give much greater weight in its rural development strategy to the non-agricultural
elements of rural life, such as education, health, infrastructure, rural financial services (including
micro-credit), non-agricultural economic activities, and administration.

Greater emphasis on poverty alleviation. Consistent with the region’s overall strategy,
the Bank’s future operations will be more focused on poverty reduction efforts. This will require
certain adjustments of the Bank’s traditional work program, including some of the following
measures:

- Focus operations on the relatively poorer countries and on poor regions within wealthier
countries (for example, less emphasis on EU accession and more on Central Asian
countries).

- Give more attention to the issues of concern to populations in the lower-income groups
(for example, focus on efficiency measures for the crops produced by the poorer farms).

- Invest more time and resources to ensure viability of the social assets that serve the poor
(health, education, and community resources).
• Put more focus on access by the poor to land (the Bank has good models in Azerbaijan, Georgia, and Moldova), credit (e.g., in Moldova, Albania, the Kyrgyz Republic, and Latvia) and markets (Albania).

• Put greater emphasis on the poverty alleviation aspects of irrigation rehabilitation in Central Asia, Caucasus, and southern Europe.

**Community Development.** Experience with farm support services, rural infrastructure, irrigation, microcredit, and natural resources programs has indicated that projects that are planned and implemented with a high degree of local participation are generally more successful than programs that are centrally planned and implemented. There are tradeoffs here; local rural lobbying groups in the ECA region, as in OECD countries, may put barriers in the way of "economically rational" reforms. Nevertheless, transparency at every stage generally improves the chances of success of these reforms.

**Country Strategies**

The Bank intends to be active in all countries of the region where Bank assistance is requested, and the conditions for the Bank’s involvement, according to its principles and rules, are feasible. Accordingly, it is most likely that the Bank will have its most significant role in the Caucasus, Central Asia, and in southeastern Europe. The Bank considers the graduation of the EU accession countries of Central Europe as an indication of progress both for the World Bank and the countries themselves. The most significant challenge remaining is the core of the CIS—Russia, Ukraine, and Belarus—where the Bank’s involvement in the future will increase only if significant change in political will is evident for implementing serious and comprehensive reforms in the rural sector. A summary of areas for emphasis and possible areas for World Bank support by subregion are presented in tables 2 and 3.
INTRODUCTION

Agriculture and the rural sector in general play a more important role in the economy of the Europe and Central Asia (ECA) region than they do in more-developed market economies. The rural sectors in Central and Eastern Europe and Central Asia are undergoing systemic changes. The Bank strategy for rural development in the ECA region during the early phase of transition emphasized the reform of agricultural policies and assistance in privatizing, restructuring, and rebuilding agriculture and agro-industrial complexes. Given the developments of the past decade, it is clear, however, that the initial expectations for the outcomes of such reforms were overly optimistic. The transition process in agriculture is far more complex than originally envisaged by both the countries themselves and the international community, including the Bank. Increased social problems and the alarming growth of poverty have added a new, unexpected dimension to the transition process. As the forthcoming analysis indicates, the region's rural economy is still struggling to adjust to new economic realities, and this will require further refinement and adjustment of the Bank approach as well.

This paper, based on an overview of recent regional developments, summarizes the revised World Bank assistance strategy for rural development in the ECA region. The rural sector includes the people; the economic development activities; the institutional, economic, and social infrastructure; and the natural resources of rural areas, and is thus not confined to agriculture alone. This chapter focuses on Bank activities that support rural development and policy reforms designed to improve rural well-being and increase the competitiveness of all rural enterprises. Natural resources and social issues are addressed in separate chapters.
I. THE STATE OF AGRICULTURE AND THE RURAL ECONOMY

A. Agriculture and Food Production: Stagnation and Decline

Retaining a Significant Role in the National Economy

The transition region has a substantial part of the world’s agricultural resources (figure 1). In the mid-1990s the countries concerned comprised 13 percent of the world’s area suitable for agricultural production\(^1\) and 19 percent of arable land.\(^2\) The region makes a substantial contribution to world output in practically all of the main agricultural products. On average, this contribution is around 10 percent (figure 2).

Considering its natural resources, the region plays a small, but important role in the world food trade (figure 3). Around 20 percent of the potential world food production resources are located in the region, but only 7 percent of the world’s population. It is thus perhaps the one region in the world in which a good deal of the substantial global food demand that is forecast for the first half of this century can be met without the risk of causing serious harm to the natural environment.

The share of agriculture in employment and national income in ECA countries is far greater than the average for Western developed countries. In 1997–98 the agrarian sector contributed about 9 percent of GDP for the transition region as a whole,\(^3\) while the proportion of the agricultural population was 16 percent.\(^4\) However, there are very substantial deviations from country to country. The share of agriculture in GDP is only 5 percent in the European Union (EU) accession candidate countries, compared to 31 percent in the Caucasus, and 24 percent in Central Asia.\(^5\) The contribution of agriculture to GDP is much lower than the role it plays in

\(^{1}\) 1994.
\(^{2}\) 1996.
\(^{3}\) World Development Indicators (WDI) World Bank, 1999.
\(^{4}\) Food and Agriculture Organization (FAO).
\(^{5}\) WDI.
employment. This is an indication of the low productivity of agriculture and of efficiency below the developed country average.

Figure 2. Production of ECA Transition Countries (TC) in Comparison to World Production, 1992–93 and 1998–99

Declining or Stagnating Outputs

The agrarian economy of the region in the 1990s was characterized by a considerable fall in production. This decline reflects the impact of a wide variety of changes, including drops in demand, a reduction in producer subsidization, the collapse of traditional export markets and the internal “Eastern Bloc” trading system, and deteriorating machinery stock.

The major developments in production performance can be summarized as follows:

- Between 1990 and 1996, the share of GDP produced in agriculture at the regional level fell annually at an average of 7.8 percent, and in 1997 it declined both in the Commonwealth of Independent States (CIS) and Central and Eastern Europe (CEE) to 11 percent and 6 percent, respectively (which is a rate of decline that was greater than that of the rest of the economy).6
The decline in agricultural production continued in the late 1990s in most of the CIS countries. Kazakhstan experienced a particularly poor harvest in 1998, as did Russia and Ukraine in both 1998 and 1999. (figure 4).

The output of all major products in the CIS has remained significantly below the pre-reform levels. In 1998–99 there were, however, signs of recovery in crop production, especially for fruits and vegetables. At the same time, the outputs of all major livestock products continued to decline, indicating a deepening crisis in the livestock sector in the CIS countries.

In contrast to the CIS, signs of output stabilization can be observed in the CEE countries. In most cases this stabilization occurred at 70 percent to 100 percent of the pre-reform levels, while in Estonia, Latvia, and Croatia, current production appears to have stabilized at 40 percent of pre-reform output (figure 5).

During the 1990s there was a decline in the contribution of the region and the two main subregions (CIS and CEE) to world output with regard to the main agricultural products. The sharply declining shares of CIS countries in the global output of major agricultural products during the last two years reflect the increasing gap between global agricultural development and the performance of these countries. The decline in contribution can be observed even in the CEE countries, indicating that the overall performance of the CEE countries has also remained below world averages.
Lack of Productivity Gains

An international comparison of cereal yields confirms the assessment provided above (figure 6). In the CIS countries, there is a declining trend in major grain yields. The decline is especially significant in countries that lag behind in agricultural reforms, namely, Russia, Ukraine, and Belarus. In CEE countries, grain yields have shown a stagnating trend in the last five years, with much less annual variation than the CIS countries.

Agricultural technology levels did not improve in 1997–99 in any measurable way. For the region as a whole, the use of agricultural inputs remained at about the level of previous years, which is only about 15 percent to 20 percent of pre-reform levels. Figure 7 shows the major indicators of fertilizer use. An upward trend can be observed only in CEE countries.

Increased Integration into Global Trading System

The regional participation in international trade of agricultural products has undergone a significant change during the transition. Despite the decline in production, the region’s share of world trade did not shrink substantially, and, in the case of some products, there was even an increase in trade with the rest of the world. This was made possible (or required) by the fall in
domestic consumption and by the disintegration of the Soviet Union. In some countries there has been considerable change in the composition of agricultural trading partners. The region’s agrarian trade was historically determined by the CMEA and built on internal relations. It has now given way to a wide opening toward other parts of the world. Conversely, growth in most CIS countries is seriously constrained by the collapse of traditional markets and failure to develop alternatives.

Despite the considerable change in the structure of the region’s agricultural exports and imports (as a result of declining consumption), the balance of agricultural trade for the region as a whole has not deteriorated. Overall, the region continues to be a net importer of agricultural products, although the deficit is declining. On the regional level, the impact of the significant reduction in the negative trade balance of the CIS countries has been partially offset by the increased deficit in the CEE (figure 8).

The source of imports and destination of exports have also changed. Perhaps the most significant structural change is that the CIS countries, particularly Russia, have become one of
the world’s biggest meat-importing regions. In place of the massive grain imports characteristic of the Soviet period, Russia now mainly buys meat. This is quite clearly a more favorable outcome from an economic viewpoint since the large quantity of grain purchased in earlier decades by the Soviet Union was used in animal husbandry with very low efficiency. At the same time the CIS countries are increasingly appearing on world markets as grain exporters.
On the whole, the region's agrarian trade is becoming steadily integrated into the agrarian trade of the world and the European region. This process is most advanced in the case of the countries of Central and Eastern Europe where the CEFTA offers further, but not problem-free, possibilities for regional cooperation. In most of the countries concerned, a liberal agrarian trade policy is also assisting in the integration of the countries into world agrarian markets. Most of the countries in the Central and East European region are members of the World Trade Organization (WTO), or their admission is pending. The obligations accompanying the anticipated EU membership for most of these countries are also having a growing influence on their trade policy.

B. The Nonagricultural Components of the Rural Sector: Deteriorating Conditions

In the CIS the nonagricultural components of the rural sector during the socialist era were controlled mostly by the large-scale agricultural collective and state farms. These farms provided frameworks not only for agricultural production but also for rural social services and managed the rural nonagricultural service and production activities as well. The situation in Central Europe was different in this regard. Rural social services (schools, health services, housing, and so on) remained independent of the large-scale farming sector, though these farms occasionally contributed resources to these services.
The overall development policies in the region were focused primarily on urban industrial areas during the Soviet era. Basic services such as water supply, sewage systems, telecommunications, and so on were also relatively well developed in larger villages, but not in the countryside. The level of development in rural social services and nonagricultural rural activities has differed in various parts of the region. Central Europe and the western part of the former Soviet Union (especially the Baltics and Belarus) have made significant improvements in rural infrastructure and social service provision. A few Central European countries have even maintained a small-scale, private nonagricultural rural service sector. In most of Russia and Central Asia, however, rural social services and infrastructure have remained relatively underdeveloped, as indicated by the lack of access to water and sanitation (figures 9 and 10). Services outside of the large-scale farms virtually do not exist in these regions.

Figure 9. Access to Improved Water, 1993–95

Since the beginning of the transition, there has been an overall deterioration of the rural nonagricultural situation throughout the CIS. The actual dismantling of large-scale farms or the deteriorating financial conditions of the remaining ones has significantly reduced the resources available for social services and rural infrastructure. In some places the responsibility for these tasks has been transferred to the municipalities, but the question of their financing is still mainly unresolved, and thus they remain underfunded. An economically declining rural environment has also significantly retarded the emergence of a private-based rural nonagricultural sector.

The situation in Central and Eastern Europe is considerably better. The initial state of rural nonagricultural conditions was significantly more developed and much less affected during the reform years. In a number of Central European countries, such as Hungary, the Czech Republic, Poland (with the exception of some underdeveloped areas, such as southeastern Poland) and the Baltics, a visible recovery of rural nonagricultural activities can be observed.
This recovery is driven by the private sector and local municipalities, which are gaining increased fiscal and legal autonomy. The resumption of overall growth in these countries and the decline in unemployment have had a positive impact on the rural sector.

**Figure 10. Access to Sanitation, 1993–95**

![Bar chart showing access to sanitation in rural and urban areas of various countries.

C. Increased Rural Poverty and Social Problems

Since the beginning of the transition, there has been a sharp rise in national poverty and inequality in ECA countries. National poverty incidence has reached very high percentages in many countries, according to recent World Bank poverty assessments. Rural poverty has increased in line with the rise in national poverty, if not more so. This is due to the large size of rural populations within ECA (43 percent of total country population, on average—see table 1) and the high dependence of rural households on agricultural income. Of the 404 million inhabitants in the 26 ECA countries (excluding Turkey), 142 million, or 35 percent, are classified as living in rural areas. Six countries have particularly large rural populations, accounting for slightly more than two-thirds of the total rural population within ECA. These are Russia (the largest contributor, at 25 percent), Ukraine (contributing 15 percent), Poland (9 percent), Uzbekistan (8 percent), Romania (6 percent) and Kazakhstan (5 percent). In the less-developed countries of Central Asia, the majority of the population lives in rural areas. Tajikistan, with 67 percent rural population, represents the extreme in this regard.

Rural poverty is an important contributor to overall poverty in a large number of ECA countries. Figure 11 shows rural poverty indicators for about 20 ECA countries for which recent data are available. Some caveats are necessary, however:

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6 World Bank, *Poverty Trends and Voices of the Poor*. 
Most poverty assessments show that the poor are closely grouped above and below the poverty line, making poverty estimates sensitive to small changes in the poverty line or small changes in economic conditions.

Single-year estimates of poverty (such as those in Figure 11) should be interpreted with caution because they are likely to change with small changes in economic conditions.

This clustering phenomenon should also raise concern about groups such as the rural elderly, which, although typically above the poverty line (because of pension transfers), might easily fall below the line with a change in economic circumstances.

Table 1. The Significance of Rural Populations in ECA

<table>
<thead>
<tr>
<th>Country</th>
<th>Rural population as percentage of ECA's total rural population</th>
<th>Rural population as percentage of country's total population</th>
</tr>
</thead>
<tbody>
<tr>
<td>Russian Federation</td>
<td>22.4</td>
<td>32.8</td>
</tr>
<tr>
<td>Turkey</td>
<td>11.7</td>
<td>28.4</td>
</tr>
<tr>
<td>Ukraine</td>
<td>9.6</td>
<td>47.9</td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>8.9</td>
<td>58.3</td>
</tr>
<tr>
<td>Poland</td>
<td>8.9</td>
<td>38.9</td>
</tr>
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Source: FAO
Table 2. National and Rural Poverty Indicators for ECA

<table>
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<tr>
<th>Country</th>
<th>GNP per capita ($)</th>
<th>National incidence (absolute poverty line: $4.30/day) (%)</th>
<th>Ratio of rural to urban poverty incidence (relative poverty line) (%)</th>
<th>Contribution of rural poverty to total poverty (relative poverty line) (%)</th>
<th>Year of survey</th>
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<td>0.7–3.9</td>
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</table>

Sources: For column (a), World Development Indicators; for column (b) - ; for column (c)–(d), ECAPOV study calculations on LSMS surveys.

With these observations in mind, a number of conclusions can be drawn about the importance of rural versus urban poverty:
Within 15 of the 20 ECA countries for which poverty data are available, the incidence of poverty in rural areas is as high or higher than in urban areas. On average, for all countries, rural poverty incidence is 60 percent higher than urban incidence.

Because urban populations tend to be larger than rural populations, the contribution of rural areas to the total number of poor is less. Even so, in 10 of the 20 ECA countries, the rural poor account for as much of the total poor population as the urban poor do (see column [d] of table 2). On average, the rural/urban contributions are equal.

Some other subregional patterns are worth mentioning. Data are available for three of the five Central Asian countries (Kyrgyz Republic, Tajikistan, and Kazakhstan), and this is the one ECA subregion in which rural poverty appears to dominate the poverty profile. Central and Eastern Europe countries show a mixed pattern, with some countries exhibiting a very high rural poverty contribution to the total poverty profile (Poland, Romania, Macedonia) and some very low (Slovenia and the Czech Republic).

One conclusion to be drawn from figure 11 is that an attack on total poverty in a given country will frequently require sustained attention to rural poverty. However, activities that reduce poverty in small countries may not contribute much to poverty reduction in ECA as a whole. ECA has approximately 136 million rural inhabitants. Rural populations are heavily concentrated in seven countries: Russia, Turkey, Ukraine, Uzbekistan, Poland, and Kazakhstan (table 1). These countries account for about one-quarter of the ECA countries but almost three-
quarters of the total rural population. Any attempt to reduce rural poverty in ECA as a whole must therefore place some emphasis on poverty reduction in the rural sectors of these countries. A rural poverty reduction strategy needs to find a balance between attention to poverty reduction in the many individual countries where rural incidence rates and rural population shares are high, and a more narrow focus on the few countries contributing most significantly to total rural poverty in ECA. Clearly, reduction in total poverty also requires attention to urban areas, particularly in Russia and Ukraine.

It should also be mentioned that the distinction between rural and urban areas is an administrative one, often rather arbitrarily made, and different countries may classify locations as "rural" on the basis of very different criteria. This issue has not been examined systematically across countries but warrants further attention. Adjustments in the definition of what is rural could affect quantitative estimates of rural/urban poverty. These measurement issues aside, there are important qualitative differences between rural and urban poverty, such as those captured in a poverty assessment for Ukraine (box 1).

**Box 1. Rural and Urban Poverty in Ukraine**

In Ukraine, household survey data suggest that urban poverty is more frequent and deeper than is rural poverty. To a large extent, this reflects the importance of food that is produced on a household's family plot. More rural households have plots (59 percent) than do urban households (29.5 percent) or semi-urban households (11 percent), and the average size of rural plots is slightly larger than urban plots (0.33 versus 0.28 hectares).

However, to conclude that urban poverty is much worse than rural poverty may be an oversimplification. The nature of poverty in the two kinds of locations is different. In urban areas, the availability of food is undoubtedly the worst problem; poor urban households are food-poor. In rural areas, however, poor households are cash-poor. Buying bread, let alone clothing, winter heat, medicine, educational supplies, or transportation, may be out of the question. The rural poor are better off in terms of food, but the urban poor are better off in terms of everything else.

*Source: Consultations with the poor.*
II. THE REFORM PROCESS IN THE RURAL SECTOR

The relative inefficiency of agriculture is one of the most important challenges facing the countries of the former Soviet Union and Central and Eastern Europe. During the socialist era, agriculture and food production were determined by government planning, without regard to efficiency or comparative advantage. The large-scale livestock and crop cooperatives were unsuited to market-based private agriculture. Creating viable private farming based on private ownership of land and allowing market signals to determine levels and types of production have been some of the most difficult tasks of the transition period.

A. Current Status: Remarkable Progress in Central and Eastern Europe—Reform Fatigue in the CIS

In 1990–91 the region set out on the path of creating market economies based on private property. In all countries the most important basic elements of the reform process have been:

- The liberalization of prices and markets and the creation of a market-compatible system of incentives in the agrarian economy
- The privatization of land and transformation of the inherited farming structure
- The demonopolization and privatization of food processing and the trade in agricultural produce and capital goods
- The creation of a functioning rural banking system and the establishment of the institutional structure and system of state administration required by market economies.

There has been little difference between one country and another in terms of what needs to be done. However, there are big differences when it comes to the pace of realization and the manner of implementation. The results of the analysis are summarized in Table 3.1

Analysis of the reform performance for individual countries in 1997–1998 indicates a significant differentiation among CEE and CIS countries in the pace of agricultural reform:

---

1 The description of the status of reforms for each country matrix was compiled by the World Bank staff most familiar with that country’s agricultural policies. Numerical ratings were then assigned to each of the five reform categories in accordance with the criteria listed in Table 1 of the Annex. These ratings were then revised in several review sessions to improve consistency of rankings. An earlier version of this analysis was presented in Csaki and Lerman, 1997.
Table 3. Status of Agricultural Reforms in CEE and CIS Countries in March 2000
(1 = Centrally Planned Economy and 10 = Completed Market Reforms)*

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<th>Year</th>
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<th>Land reform</th>
<th>Agro-processing</th>
<th>Rural finance</th>
<th>Institutional</th>
<th>Total score</th>
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</table>

* An explanation of the numerical ratings is given in Annex 1, Table 1.
Source: World Bank estimates

- In the leading CEE countries, the reform process is close to completion (figure 12). The possibility of EU membership has accelerated reforms in those countries that were lagging somewhat behind the leading EU accession candidates, most notably in Lithuania and Latvia. Romania and Bulgaria, however, have shown only modest advancement, though in Bulgaria, the process has accelerated since 1997. The agriculture policy agenda in CEE is characterized by efforts to complete the transition, to cope with the increased social problems in rural areas, and to adjust to the evolving Common Agricultural Policy (CAP). As in Western countries, the task of facilitating increased competitiveness has often been stymied by farm lobby demands to provide immediate protection in the agricultural sector and to provide income transfers to farming populations.
In recent years there has not been any significant progress in agricultural reform in the core countries of the CIS. In Russia, Ukraine, and Kazakhstan, this standstill in the reform process has contributed to the further decline in agricultural output. Some of the smaller countries in the CIS such as the Kyrgyz Republic, Moldova, and Azerbaijan, however, have taken significant steps to pursue reforms in the agricultural sector. Tajikistan, Turkmenistan, Uzbekistan, and Belarus had still not started any significant reforms.

The diverging progress in reforms is clearly manifested in the agricultural performance of the various country clusters, formed by using 1998 progress indicators. The dynamics of change in agricultural productivity, value added, and the agricultural labor force in the various country groups show three very interesting patterns of reform.

In the fast-reforming countries there has been a significant increase in agricultural labor productivity, which has allowed the labor force to shrink while maintaining relatively stable outputs. In the middle group, with stalled agricultural reforms, all three parameters show declines or stagnation. In the third group, which comprises the non-reforming countries, there has been overall stagnation, neither significant increases, or declines took place in any of the indicators (figure 13).

B. Increased Differentiation Between Central and Eastern Europe and the CIS

Progress in the main areas of transformation has been uneven throughout the region. The most visible phenomenon, however, is the rapidly increasing differentiation in the progress of reforms between Central Eastern Europe and the CIS.

Liberalization of prices and markets

Most countries (with the exception of a few CIS countries) have taken major steps in this direction. In Central and Eastern Europe, the macroeconomic environment for agriculture that is characteristic of market economies has been developed. Prices and the system of regulation are open, more or less, to world market influences. Support for agriculture and protection of internal markets has become stronger than in the first half of the 1990s. However, the level of indirect and direct supports for agriculture remains below the average for the European Union. Frequent changes made in the system of regulations represent a problem. It remains to be seen what strategy the countries preparing for EU membership will select in introducing the EU’s Common Agricultural Policy. It is a positive trend that methods directly serving efficiency and competitiveness are increasingly coming to the fore in the system of agricultural supports.

State intervention remains strong in the CIS countries, in both price formation and trade policy. In these countries, despite the frequently proclaimed direct support for agriculture, the agrarian sector suffers serious losses due to the price policy and trade restrictions (especially export controls and taxes) separating it from world markets. Calculations show that the balance of the different interventions is negative for agriculture in a number of countries. It would appear that governments are trying to make agriculture continue to bear the burden of providing cheap food for the urban population. The growing
intervention of regional authorities in the functioning of the agricultural sector is a relatively new phenomenon. This can be observed particularly in Russia and Ukraine.

**Figure 13. The Three Paths of Reform**

**Fast Reformers**
- First Cluster
- Second Cluster

**Slow Reformers**
- Third Cluster
- Fourth Cluster

**Non-reformers**
- Fifth Cluster

---

First Cluster—Hungary, Czech Republic, Slovenia, Latvia, Estonia.
Second Cluster—Poland, Lithuania, Slovak Republic, Armenia.
Third Cluster—Bulgaria, Macedonia, Croatia, Kyrgyz Republic, Albania, Moldova, Azerbaijan.
Fourth Cluster—Romania, Bosnia, Georgia, Russia, Kazakhstan, Ukraine.
Fifth Cluster—Tajikistan, Turkmenistan, Uzbekistan, Belarus.

*Note:* Clusters refer to rankings in Table 3.
Privatization of land and reorganization of the large farm units

Land reform and land ownership continues to be the subject of heated debates in practically all countries of the region, but little progress has been made in the core of the CIS. In the countries of Central and Eastern Europe, the privatization of land based on some form of restitution is largely approaching completion. The new farm structure is characterized by a varied mix of small and large units. Almost all agricultural land is privatized and a significant portion is used by individually managed smaller farms (figure 14). The remaining pieces of the state-owned units from the socialist period are also increasingly undergoing change and adapting to market economy conditions. The legal settlement of land ownership relations is not yet completed, and the establishment of land registries and the emergence of a market for land are still in the initial stages. In a few countries a heated debate is being conducted on the ownership of land by companies and foreign nationals.

![Figure 14. Share of Agricultural Land in Individual Tenure, 1997](image)

While land has formally passed into private ownership in the majority of the CIS countries (Russia, Ukraine, and Belarus), the large-unit sector remains practically untouched. The cooperatives and state farms have been transformed into share companies. However, in practice there has been no change in the real questions of substance. These large units continue to be controlled by a central management structure and operate with low efficiency and face increasing financial problems. The role of independent private farming is marginal, largely...
because of the deterrent effect of the undeveloped market relations (figure 14). Radical land reforms have been carried out in only a few countries of the former Soviet Union, as a consequence of their special political and economic situations. This is the case for Armenia and Georgia, where independent private farming now dominates the use of arable land. Here, the distribution of land carried out on the basis of family size resulted in very small farm sizes, and this has been associated with a steep decline in agricultural production for the market. There was remarkable progress in Moldova and Azerbaijan in 1998 and 1999 (which is not reflected in figure 14) in the transformation of the Kolkhoz system. In some Central Asian countries (Uzbekistan, Tajikistan, and Turkmenistan) where private ownership of land is prohibited by the constitution, the current family-based leasehold arrangements have actually created some incentives for more efficient land utilization.

At this stage, it is very difficult to draw general conclusions about the impact of land reform in the region. However, it seems that the impact of reform on agricultural labor productivity is much sharper and clearer than on land productivity represented by yields: labor productivity increased markedly since 1992 in the CEE countries (the first two groups) and declined less in the "small" CIS countries (the third group) than in the rest of the CIS (figure 15). The improvement in agricultural labor productivity has been largely due to sharp reductions of agricultural employment in the CEE countries rather than any significant growth in agricultural output. Labor migrated out of agriculture in these countries as a result of creation of alternative job opportunities in economies that were characterized by higher GDP growth rates than in Russia, Ukraine, Belarus, and Central Asia.

At present it is difficult to find empirical evidence to judge the depth of reform or transformation at the farm level in different groups of countries. To draw some general conclusions, however, we can look at the two most visible and significantly striking manifestations of differences in approach to agrarian reform across the region. One is the policy of distributing physical plots to individuals as opposed to the policy of distributing land shares in the form of paper certificates of entitlement; the other is the policy of establishing family farms versus the policy of maintaining collectives or cooperatives. The evidence is somewhat anecdotal at this stage, but it reinforces the previous conclusions from more general observations.

Ukraine is a typical country where land is privatized by means of shares, not through distribution of plots. Armenia and Moldova, however, are countries where land is privatized through distribution of physical plots. The agricultural sector in Ukraine has stagnated throughout the entire decade, despite the country's fertile land resources. Armenia has shown respectable growth since 1992, whereas Moldova palpably switched from stagnation to some
recovery after 1996, when the authorities finally agreed on a coherent land reform policy that included distribution of physical plots. Another interesting comparison can be made between individual private farmers, who left the collectivist framework to establish an independent farming operation on their own plot of land, and the rural residents who remain workers for collectives. Collective workers, despite their entitlement to dividend payments and rent on their shares, report much lower family incomes, a much lower degree of satisfaction with their well-being, and a much lower degree of optimism regarding the future than do independent private farmers. This finding is consistent in several surveys across Russia, Ukraine, and Moldova. There is something in individual initiative that appears to be much more satisfying and rewarding than in collective life.

Work on comparisons of efficiency or total factor productivity between family farms and collectives in transition countries is just beginning, at both the World Bank and other research institutions. There is still no conclusive evidence that family farms in CIS or CEE are significantly more efficient than large collectives, cooperatives, or corporate farms. Yet the available results in the CIS clearly show that the large collectives or cooperatives certainly do not outperform the newly created, full-fledged individual farms anywhere in the region (figure 16). This in itself is a finding of tremendous importance in that it contradicts the inherited socialist belief in the superiority of large-scale agriculture, a belief that to this day has many supporters in Russia, Ukraine, and other countries in the region. Recent surveys (which covered only relatively small samples and are therefore statistically insignificant) in Hungary and the Czech Republic indicate a clearly higher efficiency in the individual farming sector. In Hungary the estimated technical
efficiency of individual farms in 1998 was 16 percent above the technical efficiency of private corporate farms and 32 percent higher than technical efficiency in the cooperatives. In the Czech Republic, the technical efficiency of individual farms exceeded the level of technical efficiency of the combined cooperative and corporate farming sector by 9 percent.\(^2\)

**Privatization of the food industry and of trade in agricultural produce and capital goods for agriculture**

Although formal privatization has been accomplished, the technological modernization of agroprocessing has yet to be implemented in most of the countries. In Central and Eastern Europe, with the exception of the Baltic states, privatization of the agricultural environment has been carried out in keeping with the principles of the privatization in general, and for the most part is nearing completion. A lag can be observed in Romania, Bulgaria, and the countries formerly part of Yugoslavia. Investments of modernization are also missing. A special case is Hungary, which, as a result of the liberal privatization process, now has perhaps the most developed food industry of the region, largely as a result of substantial foreign investment.

The CIS countries opted for what, on the whole, is a less effective solution for privatization of the food industry and agricultural capital goods and commodity purchasing. In the course of privatization, unlike the other areas of the economy, priority was given to agricultural producers, giving them majority ownership of these facilities, on special terms or entirely free of charge. Contrary to expectations, this solution did not result in new, well-capitalized owners and more favorable conditions for agricultural producers. In fact, the technological decline of the food industry accelerated and because of the complicated ownership structure it became extremely difficult to involve foreign capital.

**Rural financing**

Rural financing is still one of the biggest bottlenecks. In the CEE countries, after intensive preparations and a lengthy transitional period, the financing of agriculture has improved considerably since 1994, although the new private institutions are managerially weak and financially vulnerable. This improvement is the result partly of the reforms implemented in the banking system, and partly of the credits extended by the gradually recovering food industry and the agrarian trade and capital goods supply. Finally, there has been increasingly active operation of rural credit cooperatives, and financial institutions have increased their interest in rural areas.

In the great majority of CIS countries, there is practically no functioning rural financial system similar to that in developed countries. The inherited banking system continues to provide financing for large farms and enterprises using the accustomed methods of the earlier period (state credit financing the supply of produce for state stocks). However, there are almost no provisions for the financing of the private sector. The beginnings of a microcredit system have

\(^2\) Source: Joe Swinnen
appeared in the countries most advanced in the transformation of agriculture, namely, Armenia, Georgia, Azerbaijan, and recently Moldova, and the credits extended by the processing industry are also growing.

**Institutional reforms**

Institutional reforms are proceeding more slowly than practically all other areas of reform throughout the region. Institutional reforms have accelerated in the CEE countries since 1995, stimulated by the challenges of EU accession. Despite these tangible developments, the institutional system of agriculture requires substantial further transformation in these countries. In addition to the modernization and reform of state administration, further qualitative development is required in almost all areas of the institutional systems for market agriculture, including market consulting, training, and research. Apart from minor changes, the institutional system of the former centrally planned economy continues to operate in the CIS countries and continues to act as a serious curb on the transformation of the sector. Due to the general economic recession, there are fundamental disorders in the operation of the civil service, and the underpaid and unmotivated state bureaucrats strive to supplement their incomes through corruption. Training and research centers are suffering from severe financial problems, and in some countries they receive no financial support from the government budget.

New patterns of governance and institutional functioning are emerging in the rural sectors of ECA. Many countries have restructured regional and local governments, particularly with the breakup of collective agricultural and agro-industrial enterprises that used to effectively govern political and economic life at the local level. Newly created and/or empowered local governments, however, are now struggling with a host of new obligations, but often without sufficient authority or control over funds. Throughout the region, mostly as a result of decades of state suppression of civil society and inculcation of citizen noninvolvement, the majority of these organizations remain weak, poorly organized, and concentrated in urban areas. Despite these difficulties, rural communities are taking new initiatives, both individually and collectively, and grassroots and other civil organizations are beginning to emerge in the countryside. Areas where particular progress has been made include the development of water users associations for irrigation purposes and community-based microcredit organizations based on collective guarantee arrangements.

**C. Lessons Learned**

As we view the progress of transition so far, a number of general conclusions can be made concerning the current state of agricultural reform in the region:

- The results of the reforms have not yet met original expectations. The relatively rapid growth of production that characterized the Chinese reforms has not occurred. Transformation of the economic structure has proved to be a highly complex task. This is largely due to the incomplete creation of the basic element of farming, the private farm. In the CIS, to a large extent, the inherited large-unit structure has survived the changes.
The biggest transformation has taken place in the price and market environment, while there is a substantial lag in solving the financing problems of agriculture and in the area of institutional reforms.

Due to the adoption of more comprehensive transition policies, the transformation of agriculture is most advanced in Central Europe and, in particular, in the EU candidate countries. Even here, however, reform of the agrarian sector has not yet been fully accomplished. The results of our analyses agree with the EU's finding that further reforms are needed, principally in the area of the institutional system and in the financing of agriculture. However, land reform and the transformation of the inherited farming structure is still unfinished in practically all of the countries.

The transformation of agriculture in the CIS countries is still in a relatively early stage. Distortions continue in the production, pricing, and marketing of "strategic" products, and the system of institutions and instruments of the planned economy has not yet been fully dismantled.

Many of the transition reforms in agriculture have negative impacts on living conditions and living standards of the rural population. These negative impacts have been exacerbated by the continued stagnation and decline of the overall economies in many countries. This increase in rural poverty has surprised country governments, and its extent has also not been anticipated by the international community.

Many valuable conclusions can also be drawn from the analysis of the experiences of the countries leading the transformation, including the following:

The general economic upswing will likely help governments to undertake agricultural reforms. The greatest progress has been made in transformation of the sector by those countries where the general economic recovery has also begun.

Development in the nonagricultural segment of the rural economy is of key importance to the recovery of agriculture. In the great majority of the countries most advanced in reform, it has been the upswing of the rural economy surrounding agriculture that has made possible a substantial reduction in the numbers of people employed in agriculture and, at the same time, an improvement in the efficiency and competitiveness of agriculture itself.

An important factor in the successes achieved in reforms is consistency, and the combined implementation of parallel steps in areas related to reforms (for example, changing the whole incentive package in agriculture).

The greatest reform progress has been made by those countries that are reforming in very large steps, despite the great difficulties that these efforts are causing in the short term.

In all countries the process of agricultural reforms has been strongly influenced by day-to-day politics. Very often, politics have been and still are determining the pace and extent of
reforms, at the expense of economic rationality. In general, there is a lack of carefully considered, long-term strategies and of an objective, realistic evaluation of the economic consequences of the different possible solutions. As a result, the negative economic consequences of the transformation are greater than the unavoidable minimum, even in the most advanced countries.
III. WORLD BANK'S CONTRIBUTION TO RURAL DEVELOPMENT IN EASTERN EUROPE AND CENTRAL ASIA

A. Bank’s Rural Strategy for ECA as Embodied in Country Assistance Strategies

The Bank’s rural strategy for ECA during the past several years has reflected the overall objectives of the Bank action plan “From Vision to Action” in rural development, as well as the specific conditions in the countries of the region. The Bank’s overall strategy defined poverty reduction, widely shared growth, and sustainable natural resource management as the major overall objectives for all regions. In the ECA region, the Country Assistance Strategies (CASs) have emphasized reform of agricultural policies and assistance in restructuring and rebuilding agriculture and agro-industrial complexes. The Bank has also supported EU accession in the western part of the region. More recent Country Assistance Strategies have begun to treat rural development more comprehensively, broadening the interventions to include microcredit, rural infrastructure, and rural development more generally.

B. The Existing Portfolio

The existing loan portfolio in ECA countries consists of 55 rural and natural resource projects, with a total of $2.2 billion in IBRD/IDA commitments. Out of the committed amount, $1.8 billion has been disbursed (figures 17 and 18). One of the striking features of the rural development portfolio is the diversity of activities that fall within this rubric. There are probably more distinctly different types of activities carried out under the heading of rural development than under any other heading (figure 19). These include, for example, agricultural sector adjustment loans; land titling, registration, and cadastre; farm privatization and restructuring; rural finance and microcredit; research and extension and rural advisory services; rural infrastructure; irrigation, drainage and dam safety; forestry; biodiversity; water resource management; flood control; livestock and animal health; agro-industry and marketing; crop protection; and general rural development (including social services and infrastructure). The lessons learned from the implementation of this program are discussed below.

Figure 17. Number of Rural and Natural Resource Management Loans to Date by Year

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>1991</td>
<td>0</td>
</tr>
<tr>
<td>1992</td>
<td>20</td>
</tr>
<tr>
<td>1993</td>
<td>30</td>
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<td>1994</td>
<td>40</td>
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<td>1997</td>
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<td>1998</td>
<td>80</td>
</tr>
<tr>
<td>1999</td>
<td>90</td>
</tr>
</tbody>
</table>
Economic and Agriculture Policy Reform

Reform of economic and agriculture policies in ECA countries is a prerequisite for significant investment lending to the agricultural sector. Such reforms involve trade and price reforms, privatization, de-monopolization and deregulation of agricultural processing, marketing, and input supply. Structural adjustment and agricultural adjustment lending have been undertaken to support the above reforms in Poland, Albania, Ukraine, Romania, and Bulgaria. Agricultural issues have been important components of structural adjustment loans (SALs) in Moldova, Macedonia, Albania, and the Kyrgyz Republic. We have also used our economic and sector work (ESW), technical assistance, and adaptable program loans (APLs) to support further
policy reforms. ECA region staff monitor the state of agricultural policy reform in each country and publish an annual report of results.

The Bank has provided critical intellectual support in designing agricultural reform programs throughout the region. It has contributed to the progress in economic and agricultural policy reform of Poland, Hungary, Georgia, Latvia, Moldova, the Kyrgyz Republic, Armenia, Azerbaijan, Albania, Lithuania, and Estonia. This contribution has been carried out through analytical work, policy advice, and adjustment and investment lending to these countries.

The greatest disappointment, however, has been the slow pace of reforms in agricultural policy and rural institutions in much of Central Asia, Ukraine, Belarus, and Russia. In these countries the World Bank has not succeeded through economic and sector work and Bank dialogue in convincing governments to launch serious agricultural policy reform, nor to improve the content of their public investment programs affecting rural areas. In this group of countries, governments are reluctant to allow the widespread allocation of land ownership to private household farms. Collective and state farms continue to operate, although in some of these countries they have transformed into enterprises with ambiguous ownership. The few projects that the Bank supports in these countries are generally less effective as a result of this poor environment. In these countries, the Bank is confined to pilot projects and to projects that can be insulated to a large extent from the poor policy environment.

**Land Reform and the Creation of Efficient Farms**

Land reform and the breakup and transfer of state and socialist farms to the private sector comprise another important set of priorities in the transition to market economics. ECSSD has facilitated efforts in these areas by supporting farm privatization, establishment of cadastres, land titling and registration, and other measures to create land markets. Projects of this nature are either under way or under preparation in Bulgaria, Armenia, Estonia, Croatia, Slovenia, Uzbekistan, Kazakhstan, Ukraine, Tajikistan, Azerbaijan, Russia, Romania, the Kyrgyz Republic, Latvia, Lithuania, and Georgia. The region has been monitoring the progress in farm privatization in the major countries of the region since the beginning of the 1990s through several individual country studies and some regional comparative work identifying best practices.

The Bank’s accomplishments in the areas of land reform and the privatization of state and collective farms are probably among its greatest successes, although there is great variation in the degree of privatization of agricultural land in ECA. The Bank has achieved its successes using a combination of investment projects, adjustment lending, and sector work. Despite good progress in more than half the countries of the region, the Bank has still failed to make significant improvements in this area in Russia, Ukraine, Belarus, and most of Central Asia.

**Agricultural Services**

The Bank has played an important role in helping the agricultural economies in transition, not only with their privatization programs and the encouragement of new private farms and
enterprises but also in helping governments to identify the critical services that should be provided by the public sector. In agriculture, some of the principal public services include applied research, extension, and protection of animal health. The Bank has supported governments in reorienting their public services toward the new private farm sector, which has very different needs from the old state and collective farm structures of the Soviet period. The Bank has also supported the inclusion of advisory services that help new private farmers get information on business and financial management, in addition to more traditional technical messages. The Bank has helped establish efficient partial cost recovery systems for these services where appropriate. The Bank has supported rural services in Croatia, Macedonia, Georgia, Romania, Macedonia, Estonia, Latvia, Russia, Turkey, the Kyrgyz Republic, Azerbaijan, and Armenia. In Macedonia and Turkey, farmers are beginning to pay for their own extension services. A Bank-financed project in Estonia has helped set up an extension system based on private sector extension agents, paid for by both government and farmers. A consortium of International Agricultural Research Centers and donors is being supported by the Bank to restructure agricultural research in Central Asia and the Caucasus using regional resources and strategic compact funds.

Agro-Industry and Marketing

Although privatization of agro-industry and agricultural marketing have progressed in many countries, most privatized agroprocessing companies are proving to be nonviable, and marketing services for both inputs and outputs remain undeveloped, particularly in the CIS. This is an area where the Bank has done very little and is still trying to identify the most effective means to help develop support for what is primarily a private sector activity. Currently there are only a few Bank projects that provide support to agro-industry. These include seeds industry projects in Ukraine and Russia, a seeds component in the Agricultural Service Project for the Kyrgyz Republic, and a cotton project in Uzbekistan. There has been an attempt to develop guarantee facilities to encourage foreign agricultural input suppliers to enter the region (in the Ukraine pre-export guarantee facility (PGF)) that so far has not been successful. The Bank has also financed several wholesale markets in Poland and is supporting the development of warehouse receipts systems in Romania, Bulgaria, and Kazakhstan.

Rural Finance

Rural financial services deteriorated dramatically after independence with the collapse of the large, state-owned agricultural banks. Early efforts by the Bank to finance rural credit primarily used state banks as intermediaries. These efforts often failed, as these banks had neither the business culture nor competence to act as commercial banking establishments. Few projects supported true rural financial services; rather, most were simply lines of credit to farmers. Learning from these lessons, the Bank shifted its focus toward two approaches: (a) creating interim but sustainable non-bank intermediaries; and, (b) addressing the reasons that private banks do not lend to agriculture and rural areas. In Latvia and the Kyrgyz Republic, the Bank created Agricultural Finance Corporations (AFCs) that operate on commercial principles as a temporary measure until the banking system was ready to intermediate funds to rural areas. In
Latvia the AFC has already been absorbed by the commercial banking sector. In Albania, Moldova, Georgia, and Azerbaijan, the Bank has developed savings and credit associations that can reduce the costs and risks of small-scale and rural lending through local screening of projects and borrowers and through the substitution of social capital for physical collateral. Early experience in these countries has been quite positive. In several other countries, the Bank has concentrated on improving the lending environment and the capacity of commercial banks in the rural sector, especially focusing on developing the framework for using moveable property in secured transactions and improvement of the leasing laws. A rural finance strategy is under preparation.

Rural Infrastructure

Rural infrastructure upgrading and maintenance projects have been supported by the Bank and implemented by private contractors and local communities in partnership with local government. Models for supporting rural infrastructure development, with a focus on rural roads, rural water supply, and rural energy, are underway in Poland and Albania, and a project is being prepared in Romania. The Poland Emergency Flood Relief Project sent to the Board in FY2000 assists in rehabilitation of rural infrastructure. The more conventional approach to supporting infrastructure development, through public agencies using force account works, is discouraged. Emphasis is now put on supporting community or privately managed infrastructure at the local level.

Irrigation and Drainage

Experience worldwide is demonstrating effective ways of divesting government from the burden of irrigation costs, and lessons are being built into the design of projects under preparation in Uzbekistan, the Kyrgyz Republic, Azerbaijan, Kazakhstan, Romania, Turkey, Albania, Turkmenistan, Moldova, Georgia, and Armenia. Several irrigation projects are under way in Turkey, Estonia, Macedonia, Slovenia, and Central Asia that have had a positive impact on farm incomes and agricultural production. An important component of the Bank’s achievements is its contribution to the rehabilitation of critically important irrigation facilities in Central Asia and the Caucasus. Through its lending, the Bank has assisted in transferring management of some of the on-farm irrigation facilities in Turkey and Armenia to farmers organized in Water User Associations. This is increasing the efficiency and sustainability of irrigation schemes in both countries. However, the Bank, along with other donors, has not had a significant impact on rehabilitating irrigation elsewhere in the region. The magnitude of the problem and the cost of remediation are so large that solutions will require a strong international partnership of significant dimensions.

Accession to the European Union

The Bank has been providing assistance to the 10 Central European candidates to the European Union, helping them to introduce policies that will permit accession without
compromising efficiency and competitiveness in their agricultural sectors. This is being done through a combination of projects (such as the Poland Rural Development Project), sector work, and technical assistance. The food and agricultural sectors of accession countries are being reviewed as part of the preparation of Country Economic Memoranda (CEMs) focused on EU accession. A large regional studies program now under way and supported by the Rural Strategic Compact, is aimed at assisting the countries now being considered for membership in the European Union. The centerpiece of this program is a series of regional seminars backed by analytical studies covering various aspects of the preparation for EU accession.

The nearly $2 billion that the World Bank has contributed to the rural development of ECA countries since the early 1990s is a relatively marginal amount when compared to the overall inflow of foreign capital in the region. Since most of the foreign financing has gone to non-rural areas, however, it can safely be concluded that the Bank has been one of the main outside financiers of the rural sector in the region. The Bank’s role and leverage, however, have been different in various parts of the region. Due to the slower pace of rural economic reform, the Bank’s financing, and therefore its impact, has been rather modest in the larger CIS countries, especially in Russia, Ukraine, and Belarus. In most of the “front-line” EU accession countries, such as the Czech Republic, Hungary, and Slovenia, the need for Bank financing has declined significantly, even as the countries continue to welcome the Bank’s policy advice. At the same time, the Bank’s projects have provided significant financing in the faster-reforming countries in the Caucasus, Central Asia, and the Baltics, as well as in Bulgaria and Romania. Consequently, the Bank’s impact on policy developments in these countries has been more substantial.
IV. ECA'S STRATEGY FOR ASSISTING RURAL DEVELOPMENT

A. Broad Objectives

The broad objectives for the Bank's rural development strategy are to reduce poverty and improve the rural sector's contribution to the economic, social, and environmental well-being of the population of the countries in the region. Growth of agricultural and nonagricultural rural economies in each country is the most important ingredient to achieve these objectives. Without growth, there will not be the public and private income needed for investment for long-term sectoral viability. Regionally, however, growth cannot be resumed without completing the unfinished tasks of the transition to a private ownership-based, market-oriented economy; or without improvements in the efficiency and competitiveness of both the agricultural and nonagricultural segments of the rural economy.

Neither social nor environmental objectives can be met when the income base of the population is too low to provide private individuals, businesses, and governments with adequate funds for investment purposes. In addition, making the growth as equitable as possible in its distribution, and as environmentally sustainable as possible, is also an objective. The Bank's strategy to achieve these objectives must also include targeted interventions for the rural poor, including rural social services, basic rural infrastructure, and community development projects.

The Bank's approach to rural development in the ECA region is evolving in line with the current Bank-wide approach in this area. The traditional focus on agriculture has not been adequate to bring about significant reductions in rural poverty. Rural poverty and rural development need to be considered in a cross-sectoral context because of the "connectedness" of rural residents to many economic sectors, only one of which is agriculture. Viewing rural development more holistically will have implications as to how the Bank's strategy will be structured and implemented.

The regional rural development agenda of the 1990s emphasized the transition to a market-based food and agricultural system, the need to develop an efficient private sector with appropriate public services, and the protection of natural resources. In the later stage of the transition the importance of rural communities and rural livelihoods has also been recognized. Building on lessons of the past and insights from recent poverty assessments, the region's rural development efforts in the future will focus more on people, particularly poor people, using "bottom-up" nonsectoral community participatory approaches. Rural people are not only farmers or agricultural workers. The Bank intends to widen the scope of rural development and aim to reduce poverty wherever it is found in rural areas. In the ECA region the Bank will do this in close collaboration with its colleagues in other sectors (such as infrastructure, social services, and finance) to ensure consistency with their approaches as the Bank encourages their expansion of work into rural areas.

The Bank's evolving approach to rural development will have to take into account two region-specific phenomena as well. One is the so-called "reform fatigue" of the core CIS
countries, which is likely to require some adjustments in how the Bank addresses the reform agenda. Development of more innovative approaches to working with these countries will be a key focus in the coming years. The other is the increasing diversity in the status of rural development among countries inside the region. While the Bank’s approaches have always been specific to the particular situation in individual countries, it will see more variation in its lending portfolio over the coming years. The Bank’s strategy also takes into account many of the lessons it has learned from its past successes and failures.

B. Specific Objectives: Achievement Targets

The Bank’s experience indicates that the Bank can play a significant role in reducing rural poverty and in rehabilitating the rural sector throughout the region. This role, however, will vary significantly from country to country and in various rural subsectors. Since the resources allocated to rural development will be significantly reduced over the coming years, the Bank will focus selectively on the areas in which it has a comparative advantage, where it has working models, where it is likely to have the greatest impact on the ground, and where it can best support “inclusive” growth.

C. Components of the Regional Strategy

In the future, the Bank’s approach to rural development will emphasize both on-farm and off-farm development. On-farm development will rely on a relatively traditional approach to stimulating agricultural growth, and will focus on five key areas of critical importance (listed below). The off-farm development strategy will give recognition to the fact that agriculture is but one sector in rural areas, and that all dimensions of economic development must be addressed in rural areas.

Resumption of Agricultural Growth

Reversing deteriorating agricultural performance and resuming growth to increase rural income (farm and nonfarm), as with the Bank’s previous strategy, is a fundamental means of realizing poverty reduction in the region as a whole. The Bank will continue to stress rapid policy change, to increase private land ownership, to complete privatization of processing and marketing, and to support technological change in agriculture.

- Continuation of policy reforms. A key priority remains economic and agricultural policy reform. In the CEE countries most of the critical reforms have been carried out and the Bank will continue to support refinements though its economic and sector work (ESW) and dialogue, but it does not envision any adjustment lending. In southeastern Europe some countries have made considerable progress, while in others the performance has been uneven and selective adjustment support will be required. In the CIS, the policy reform agenda remains a top priority, but adjustment lending may not be the right instrument. The Bank is currently rethinking its approach to CIS countries as they struggle with market reforms. The Bank may use a mix of World Bank Institute (WBI)
training for top officials and parliamentarians, together with very targeted ESW and selective conditions in economy-wide adjustment programs.

In general, the Bank will use the sector adjustment loan quite judiciously. Its experience with this type of lending has been mixed, with important progress in some countries and some areas but a frustrating lack of progress and sometimes backsliding in others. The Bank has struggled with the perennial problem of having agricultural ministers responsible for undertaking initiatives that are difficult administratively or politically in exchange for a very indirect payoff. The Bank has also run up against the common problem of changing economic situations and priorities that have stymied progress toward its second tranche release conditions. In the future, the Bank will be very selective in using stand-alone sector adjustment operations, deploying this instrument only for one tranche operations where actions have already been undertaken. The bulk of the Bank’s lending for policy reform will be in the form of multisectoral structural adjustment operations where agriculture and rural reforms are one component. Using all of the instruments at its disposal, however, the Bank will aim to achieve average transition scores of 6.5 (as measured in table 2) by 2004.

- Land reform and the creation of efficient farms. Land reform, particularly farm restructuring and privatization, is one of the Bank’s major priorities. The region’s track record in this area is reasonably good, and the Bank remains very active in these activities. It has covered most of the countries of the CEE, southeastern Europe, and Caucasus with support for cadastre, titling, and registration activities already, so its primary focus for the future will be in the CIS. In most of these countries, the Bank is still working on facilitating the breakup of the state and collective farms and transferring ownership of land parcels into private hands. The Bank will also provide titling and registration support to those countries that have successfully privatized individual parcels. In the next few years, through various Bank operations, the Bank aims to support the provision of land titles to at least 10 million new landowners.

- Agricultural services. New private farms have quite different needs for information and support than did their predecessor state and collective farms. The requisite delivery systems for this information and these services are also quite different. Once the state and collective farms have been restructured and have their land transferred into private ownership, the Bank will provide support for applied research, extension and advisory services, and animal health services. The Bank will continue to emphasize business and financial management advice and provision of market information, including prices.

- Agro-industry and marketing. The region has struggled to find a successful approach to providing support in this area; however, the poor performance and limited competitiveness of agroprocessing industries and marketing institutions continue to impose significant constraints on rural development. The Bank’s experiences in the seed sector have not been very encouraging, and the Bank is not likely to pursue this avenue much further. The Bank is now seeking ways to establish linkages with the IFC, other private investors, and nongovernmental organizations (NGOs) active in aiding agrobusiness development (the
Citizens Network, for example). For the time being, Bank assistance will be limited to technical assistance and to various forms of guarantee facilities.

- Irrigation. Experience in ECA and other regions shows that with irrigation, as with other previously government-owned and -operated service sectors, stakeholder control improves performance, and policy is as important as good engineering in determining the success of an investment project. Recent projects have focused not just on building new canals or rehabilitating old ones, but also on building the institutional infrastructure to ensure their efficient operation and sustainability. This has involved helping to set up associations of water users, which then assume control over the operation and maintenance of some of the infrastructure. This trend will continue and future projects will seek to transfer not only operational responsibility, but also ownership of infrastructure, along the lines of current practice in developed countries. In some cases this will require that new laws be put into place. Projects will also focus on fiscal sustainability. To some extent, this objective is supported by the transfer of operational responsibility to the users. But it will also be necessary to incorporate some degree of cost recovery of the water supplied to the users’ associations, though the degree will be a subject of some debate.

Expanding Nonagricultural Rural Development

Currently the Bank’s activities are focused to quite a large extent on traditional agricultural activities. In the forthcoming period, the Bank intends to give much greater weight in its rural development strategy to the nonagricultural elements of rural life, such as education, health, infrastructure, rural financial services (including microcredit), nonagricultural economic activities, and administration. The Bank will aim at stimulating off-farm rural enterprises and creating off-farm employment opportunities.

- Development of rural infrastructure. Rural infrastructure upgrading and maintenance will be supported, implemented by private contractors and local communities in partnership with local government. Some of the Bank’s ongoing activities in Poland, the Kyrgyz Republic, Albania, and Romania provide various models for supporting rural infrastructure development. The more conventional approach to supporting infrastructure development, through public agencies using force-account works, will be discouraged. Emphasis will be put on supporting community managed, or privately managed, infrastructure at the local level. Social funds assisting rural communities are likely to be increasingly demanded by the Bank’s clients and will be an instrument used more frequently for this type of investment. This work will be carried out in full cooperation with our Infrastructure and Human Development colleagues.

- Rural finance. The Bank continues to focus its efforts in two key areas: (1) addressing the reasons that private intermediaries are not lending to rural areas (such as high costs and risks, lack of collateral, and lack of sector knowledge); and (2) creating self-sustaining intermediaries that can provide financial services in rural areas (cooperatives, savings and credit associations, credit unions). While the Bank’s experience with public nonbank
institutions in Latvia and the Kyrgyz Republic has been very good, it does not see the need to pursue this approach any longer. The Bank either will work with the existing banking system to eliminate impediments to their commercial lending to the sector or will focus on the development of community-based microcredit institutions and retail bank outlets that can reduce the costs and risks of small-scale rural lending. The Bank will not substitute for the work of its financial sector colleagues, but will seek to complement it by helping to develop the instruments key to facilitate rural lending.

- Rehabilitating integrated rural development programs. Integrated rural development projects have not been viewed as successful in the Bank’s history. They have failed primarily because they were excessively centralized and “top down.” The development needs of rural areas in the region, however, sometimes do require an integrated approach. The EU-sponsored rural development programs, such as the Special Assistance Program for Agricultural Research and Development (SAPARD), also envisage a comprehensive treatment of rural problems. In learning from the negative experiences of the past, the Bank intends to develop and implement a new generation of integrated rural development projects based on decentralized community-based project design, implementation, and monitoring. The Bank’s first project of this type, the Poland Rural Development Project, is currently being implemented. This project was designed by a team that involved several sector units in the Bank and a large group of local stakeholders in Poland. The Bank has received interest in similar projects from several other countries. It will use the Polish experience in the design and implementation of any future projects of this nature.

- Developing rural focus in national education, health, and other social service programs. Traditionally the national-level social projects have little rural focus. The Bank intends to initiate a dialogue with its Bank counterparts in the other sector units to increase their awareness of rural conditions and problems. The Bank will call their attention to the specific needs of the rural sector and offer contributions to develop rural components for nation-wide projects.

- Expanding analytical work on nonagricultural rural activities. The analysis of the nonagricultural rural activities will be a regular component of the Bank’s ESW program. Similarly, ECA would like to pay more attention to rural-urban linkages in its analytical work. The first study of the rural nonagricultural activities is now under way, including several country case studies. In the future the Bank will expand its policy monitoring and reviewing activities beyond agriculture to include all components of the rural sector. Additionally, self-standing studies of various critical issues of the nonagricultural rural life will be initiated, both in a country and a regional context. At first, a comprehensive review of the region’s nonagricultural rural activities would be desirable.

Greater Emphasis on the Poor

Consistent with the region’s overall strategy, the Bank’s future operations will be more focused on poverty reduction efforts. This will require certain adjustments to its traditional work program, including some of the following measures.
Focus operations on the relatively poorer countries and on poor regions within wealthier countries (less on EU accession and more on Central Asia, for example).

Give more attention to the issues of concern to populations in the lower-income groups, for example, focus on efficiency measures for the crops produced by the poorer farms.

Invest more time and resources to ensure viability of the social assets that serve the poor (health, education, and community resources).

Put more focus on access by the poor to land (the Bank has good models in Azerbaijan, Georgia, and Moldova); credit (Moldova, Albania, the Kyrgyz Republic, and Latvia have good models) and markets (Albania).

Put greater emphasis on the poverty alleviation aspects of irrigation rehabilitation in Central Asia, the Caucasus, and southern Europe.

Facilitate job creation in rural areas for all economic sectors.

The greater poverty focus of the Bank’s rural development work in ECA also should include:

- Rural sector analysis with specific sections on rural poverty and its causes and solutions
- Project assessments based in part on poverty impact (positive and negative), including more social assessments; and poverty impacts monitored during implementation and preceded by baseline surveys.

**Greater Reliance on Community Development**

The Bank’s strategy considers community development as an important objective and also as a means of improving its project development and implementation. In the near future, the Bank intends to focus more in this area. Specifically, the Bank will focus on the following actions.

**Build Up the Capacity of Community Organizations in Bank Projects**

- Improve the Bank’s knowledge of local informal and formal institutions to identify the organizational bases for community development.
- Expand decisionmaking and implementation responsibilities of community groups in Bank projects.
- Strengthen the accountability mechanisms of community groups through project components.
• Build in-group revenue generation (cost recovery) and management.

• Integrate these efforts into overall advice on reform of state and municipal governments and decentralization.

Assist Government in Giving Communities a Greater Role

• Help determine the appropriate balance between government and community management of development in key sectors (such as health, education, agriculture, and infrastructure).

• Promote economic reform that transfers power and resources to local government and to community groups in a “balanced” way.

• Help local government be accountable to communities in providing elected community representation, audits, and revenue sharing.

The development of rural activities should be facilitated by various programs, such as microcredit schemes, community development grants, and rural small- and medium-sized enterprise “incubators.” Self-governance of rural communities needs to be strengthened, with increased decentralization of management and financing of public services and administration. One approach to this is the establishment of community development funds that provide resources to local communities, often on a matching grant basis, to rehabilitate or establish at the village level drinking water systems, local schools, electric power supply, rural roads, and health care centers. Communities are seeking support to upgrade rural infrastructure, particularly productive assets, in the immediate future. Experience shows that supporting community-based infrastructure in a sustainable way requires systematic efforts to consult and involve local beneficiaries concerning objectives and activities. It also requires a capacity of self-help and determination at organizing one's life. The Bank will attempt to have community consultations in every one of its projects in the ECA region.

In response to this need, it is important to establish funding mechanisms to (a) assist communities to rehabilitate or develop basic economic and social infrastructure and services at the local level; and (b) support the development of local governance structures that respond to the needs of communities in a transparent, equitable, and accountable manner. Such funds would complement, rather than duplicate other infrastructure investments, by ensuring that demands expressed by local communities do not get lost by the demands of the larger-scale programs. Community funds would finance small-scale projects identified as priorities by communities, including small-scale social and economic infrastructure (repair of primary and secondary schools, health clinics, recreational and cultural facilities, rural roads, and water systems); community services (for example, solid-waste cleanup and support programs for the elderly, the disabled, conflict widows, youth programs); business development activities (vocational or on-the-job training programs, business services, support programs for business networks); and basic community equipment (solid-waste containers and vital equipment for utilities). The Bank will aim to have some kind of community implementation in at least one quarter of its rural development projects.
D. Country Strategies

The Bank intends to be active in all countries of the region where Bank assistance is requested and the conditions for its involvement, according to the Bank’s principles and rules, is feasible. Accordingly, it is most likely that the Bank will continue to have a significant role in the Caucasus, Central Asia, and in southeastern Europe. The Bank considers the “graduation” of the EU accession countries of Central Europe as an indication of progress both for the World Bank and the countries themselves. The most significant challenge remaining is the core of the CIS, Russia, Ukraine, and Belarus, where the Bank’s involvement in the future will increase only if significant change in political will is evident to implement serious and comprehensive reforms in the rural sector.

Using the level of progress in agricultural reforms and the state of the rural economy, and obviously rates of rural poverty, as the Bank’s guide in the implementation of its strategy, the Bank will distinguish between five subregional country groupings:

1. The core of the CIS (Russia, Ukraine, and Belarus) is largely unfinished with economic transition, with huge underutilized agricultural resources and still continuously stagnating or declining rural economies.

2. Central Asia (the Kyrgyz Republic, Kazakhstan, Uzbekistan, Tajikistan, and Turkmenistan) is also largely unfinished with economic transition and all have weak agricultural sectors. The region is also experiencing significant environmental and poverty-related problems.

3. The Caucasus (Georgia, Armenia, Azerbaijan) and Moldova have made significant progress in land reform, and the agricultural sectors show the first signs of recovery. Agroprocessing and support services for private farmers are the major bottlenecks, and increased poverty is a striking phenomenon.

4. Southeastern Europe and the Balkans (Croatia, Macedonia, Albania, Romania, and Bulgaria) have made significant progress in initial reforms; however, these reforms have been affected by the continuing crisis in the Balkans.

5. Central Europe (Poland, Hungary, Czech Republic, Slovak Republic, Slovenia) and the Baltics (Estonia, Latvia, Lithuania) have the most advanced reform process, with clear signs of sectoral and rural recovery, and current efforts are focused on EU accession.

6. Turkey. Turkey is not a transition economy and has a well-developed market economy, but with some underdeveloped institutions. The two most important priorities in the rural sector currently being supported by the World Bank are comprehensive reform of the inefficient and costly agricultural support system and improvements in natural resource management.

The Bank assistance programs will be focused on the countries that are less advanced in transition and are experiencing a higher occurrence of poverty. The priority actions indicated by the Bank’s strategy for a country or country group are listed in table 4. The type of Bank operations and instruments used will be selected on the basis of the priorities listed in table 5.
Table 4. Priority Actions for Rural Development in the Region

<table>
<thead>
<tr>
<th>Priority Actions</th>
<th>CIS Core</th>
<th>Central Asia</th>
<th>Caucasus &amp; Moldova</th>
<th>Southeastern Europe</th>
<th>Central Europe &amp; Baltics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Complete macro policy reforms</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Complete land reform and create functioning land market</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Create private sector-oriented research, extension, and agricultural services</td>
<td></td>
<td></td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Rehabilitate agroprocessing</td>
<td>X</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Promote foreign direct investment</td>
<td></td>
<td></td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>Develop rural finance systems</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>Accelerate institutional reforms</td>
<td>X</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Develop rural infrastructure and social services</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Rehabilitate irrigation</td>
<td></td>
<td>X</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Prepare for EU accession</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Introduce poverty-oriented community development programs</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
</tbody>
</table>

Table 5. Priority Projects for Rural Development in the Region

<table>
<thead>
<tr>
<th>Priority Projects</th>
<th>CIS Core</th>
<th>Central Asia</th>
<th>Caucasus &amp; Moldova</th>
<th>Southeastern Europe</th>
<th>Central Europe &amp; Baltics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agricultural adjustment loans</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land reform support projects</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agricultural service projects</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Agroprocessing projects</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Guarantee projects</td>
<td></td>
<td>X</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rural finance projects</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Rural infrastructure and social service projects</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Irrigation projects</td>
<td></td>
<td>X</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Integrated rural development projects</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Rural community development projects</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td>X</td>
</tr>
</tbody>
</table>
E. Specific Issues for Project Design and Implementation

In designing and implementing the Bank’s program in ECA, there are a number of thorny issues that repeatedly arise. The Bank’s strategy seeks to provide some guidance and to at least ensure that the trade-offs are carefully considered in specific instances.

Poverty Reduction Versus Growth

In many cases, there seems to be a trade-off between interventions that are good for growth and those that reduce poverty. This dilemma arises both in the context of policy reforms and in the context of investment operations. With respect to policy reforms, the main question is whether reforms aimed at enhancing growth will have negative impacts on the poor. Clearly there are some cases in which they will. For example, removing high price supports for certain products will reduce the incomes of farmers who grow those products. Though it is well recognized that the biggest gainers in absolute terms from price supports are the relatively larger and richer farmers, some of the beneficiaries are likely to be poor, and they will lose from elimination of the supports. In this particular case, there may be a way to facilitate a solution whereby the removal of support prices can be undertaken but the poor can be protected at the same time. For example, a safety net of some kind could be introduced, perhaps with specific features that make it relevant for poor farmers who are often missed by such programs. Or since there are few programs that can successfully do this in remote rural areas, other options could be considered, for example, a system of direct income support payments might be established (that is, per-beneficiary transfer payments that are decoupled from levels of input use or output). We will seek to find win-win solutions and will choose, as priorities, to address reforms where we can also mitigate the impact on the poor. In order of priority, we will emphasize (1) reforms that are good for growth and improve the well-being of the poor (for example, the removal of state orders); (2) reforms that are good for growth and for which offsetting interventions to protect the poor can be established (such as transfer payments as discussed above); and (3) reforms that are good for many poor, even if they have a negative effect on other poor (for example, the increase in producer prices for staple crops consumed by urban poor). The Bank will minimize emphasis on reforms that are bad for the poor when there are no means to offset or compensate the impact.

There are also trade-offs between growth and poverty alleviation in the selection and design of investment operations. Some projects may have a very high rate of return, but benefit mainly relatively high-income groups, and vice versa. Of course, the use of “Squire and van der Tak” type analysis to calculate rates of return (whereby distributional weights are added to the various costs and benefits) could be used to determine the choice of projects. In practice, however, this approach has not proved to be very practical. There are problems with determining the weights, and many of the typical World Bank investments do not lend themselves easily to traditional cost-benefit analysis. When cost-effectiveness analysis is used, quantitative distributional weights are difficult to apply.

It should be recognized that taking distributional effects into account may lead us to select projects that do not necessarily have the highest economic rate of return or make the highest contribution possible to growth. If the best way to reduce poverty is to encourage
ECA’s Strategy for Assisting Rural Development

45

economy-wide growth, then systematically making low-growth choices may not be in the best interests of the poor. However, recognizing distributional considerations will ensure that growth is more inclusive. In the Bank’s project choice, it will choose interventions that generate the highest possible inclusive growth.

Social Objectives Versus Financial Viability

Another strategic issue for the Bank has been determining the appropriate level of cost recovery. Typically, public investments made for purely private benefit should be fully financed by the ultimate beneficiary, and “public goods” should be financed by the public expenditure budget. In practice, however, such questions are always more complicated. For example, many ECA governments are now considering borrowing from the Bank to finance rehabilitation of their irrigation infrastructure. In the context of such projects, the Bank is helping governments to determine the degree to which cost recovery should be required.

Many of these irrigation projects will generate purely private returns for individual farmers. If the investments are estimated to increase farmers’ incomes by more than the associated costs, the farmers should be willing and able to pay at least part of this amount in the form of water charges, particularly if they gain better control over the water through water users associations. But several arguments arise as to why there should not be full cost recovery on these investments. Even when financial rates of return show that farmers should be able to cover some, if not all, of the costs associated with their new investment, governments have been unwilling to impose such charges. For example, when the beneficiaries are relatively poor, there may be no better system for transferring income (that is, the administrative structure for a social safety net may be nonexistent). Also, irrigation is a good way to help poor farmers reduce risk and in the absence of other, market-based mechanisms, financing irrigation infrastructure may be an appropriate means for governments to provide this kind of support.

A second set of issues arises when the financial returns from the irrigation project are not high enough to allow farmers to cover the incremental costs of the new investment. Prima facie, there would be no case for the project. But in many instances, it can be argued that, in the absence of the project, the irrigation infrastructure would deteriorate to such an extent that there would be significant out-migration from rural areas. Such migration could bring extremely high costs of social dislocation and congestion in the cities. This argument is especially pervasive in Central Asia, where farming would be nonviable under rain-fed conditions, where hundreds of thousands of people, perhaps millions, are dependent on the irrigation infrastructure, and where the cities are ill-equipped to receive large numbers of immigrants. In such a case, the cost to the economy to fund the money-losing irrigation project might be less that the cost to the economy of mass migration from the rural areas in the absence of the project. An analysis based strictly on financial viability would clearly show that the project should not be done, while if the social externalities are included, it could very well pass an economic cost-benefit test.

In these cases, the Bank must sensibly quantify and incorporate the social costs and benefits of both “with” and “without” project scenarios. The Region must recognize that the simple existence of these costs does not imply that all such projects make sense. Projects that
pass the economic cost-benefit test (including social cost benefits) should also have to pass a "reasonable alternatives" test that would examine other options for handling the social costs. It might, for example, be less expensive and more beneficial to help farmers relocate and mitigate the resulting urban congestion costs than to carry out a large-scale, money-losing irrigation investment. This in essence is the principle of the Northern Migration Project in Russia. Another alternative might be to assist farmers to revert to (relatively unproductive) dry-land farming, and pay them an income supplement, which could be made available only to current farmers, with payments to their heirs gradually phased out after they die. Future generations would thus exit over time, not all at once. The advantage of the latter strategies over that of making the investment is that they assist in exiting an nonviable activity, while the investment gives farmers an incentive to stay in the activity permanently. The grants and mitigation expenditures could be relatively generous, since they would be given only over a finite time, while the water subsidies would be permanent. These considerations will be considered explicitly in the Bank's future irrigation projects.

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The judgment here was that it makes more sense to help people get out of places where they cannot survive without heavy energy subsidies than to rehabilitate and modernize the power plants to minimize energy costs, which even after the investment would continue to require subsidization into the indefinite future. This is an analog to the situation with the irrigation programs in Central Asia.
**ANNEX 1**

**Key to Numerical Ratings Used in Table 1**

<table>
<thead>
<tr>
<th>Market-Conforming Trade and Price Policy</th>
<th>Land Reform</th>
<th>Privatization of Agroprocessing and Input Supply</th>
<th>Rural Financial Systems</th>
<th>Public Institutional Framework</th>
</tr>
</thead>
<tbody>
<tr>
<td>3-4. Deregulation with indicative prices, and price controls; significant NTB on imports or exports.</td>
<td>3-4. Legal framework for land privatization and farm restructuring in place, implementation launched only recently</td>
<td>3-4. Spontaneous privatization and mass privatization in design of early implementation stage.</td>
<td>3-4. New banking regulations are introduced, little or no commercial banking.</td>
<td>3-4. Modest restructuring of government and public institutions.</td>
</tr>
<tr>
<td>5-6. Mainly liberalized markets constrained by the absence of competition and some remaining controls on trade policy.</td>
<td>5-6. Advanced stage of land privatization, but large-scale farm restructuring is not fully complete.</td>
<td>5-6. Implementation of privatization programs in progress.</td>
<td>5-6. Restructuring of existing banking system, emergence of commercial banks.</td>
<td>5-6. Partly restructured governmental and local institutions.</td>
</tr>
<tr>
<td>7-8. All command economic-type interventions are removed. Market and trade policies are in compliance with WTO. However, domestic markets are not fully developed.</td>
<td>7-8. Most land is privatized, but titling is not finished and land market is not fully functioning.</td>
<td>7-8. Majority of industries are privatized, with a framework conducive for foreign direct investment.</td>
<td>7-8. Emergence of financial institutions serving agriculture.</td>
<td>7-8. Government structure has been refocused while research, extensions, and education are being reorganized.</td>
</tr>
<tr>
<td>9-10. Competitive markets with market-conforming trade and agricultural policies.</td>
<td>9-10. Farming structure based on private ownership and active land markets.</td>
<td>9-10. Privatized agro-industries and input supply, with improved international competitiveness.</td>
<td>9-10. Efficient financial system for agriculture, agro-industries, and services.</td>
<td>9-10. Efficient public institutions focused on the needs of private agriculture.</td>
</tr>
</tbody>
</table>

*Source: World Bank estimates.*
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