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INCOME DIVERSIFICATION FOR SUSTAINABLE DEVELOPMENT OF EUROPEAN AND CENTRAL ASIAN RURAL AREAS – ROLE OF THE FOOD AND AGRICULTURE ORGANIZATION OF THE UNITED NATIONS (FAO)

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I. INTRODUCTION

1. Broad changes are taking place in food and agricultural systems worldwide and farmers and rural areas across Europe and Central Asia will face significant challenges. The average income per head is still lower in rural regions than in towns and cities and the skills base is narrower and the service sector less developed in rural regions. Many rural regions across Europe now depend on a wide range of economic engines for growth. Increasing globalization, improved communications and reduced transportation costs are additional drivers of economic change in rural areas.
2. At the same time the Common Agricultural Policy (CAP) of the European Union has been amended in order to help higher economic growth, job creation and greater competitiveness in world markets as well as to provide farmers and rural communities with a better standard of living in an environmentally and socially sustainable way, which can serve as models for possible approaches to income diversification in rural areas for other countries in the region.
3. Although the nature and pace of change varies among and within countries and regions, a common characteristic in developing regions is the transition to market-driven systems associated with greater reliance on input and output markets, hence the development of competitive agriculture sectors. At the same time, agriculture has become increasingly less important as an economic driver in rural areas. Both developments, the competitive pressure and the decreased economic relevance of the sector lead to a structural change process in agriculture, increasing farm sizes and replacing labour through capital.
4. Ultimately an accelerating release of agriculture labour-force is taking place, putting at risk the livelihoods of many rural households. Creation of employment and alternative income opportunities is therefore a potential tool for creating growth and sustainable development of rural areas. Income diversification through rural enterprise development has the potential to provide employment for the rural poor in the form of off-farm activities related to agriculture production, such as handling, packaging, processing, transporting and marketing of food and agricultural produce. There is however, also a clear connection between primary production and other related economic activities in rural areas (e.g. services, infrastructure, etc.), which build a strong link between agriculture and rural development. Unfortunately, there are also risks and trade-offs, often affecting the most vulnerable countries and people and there is a number of issues, bottlenecks and challenges, that need to be addressed in order to ensure that these policies are effective and efficient.
5. It is important to build on the experiences of countries that have developed competitive agricultural sectors and vibrant rural economies in order to improve the understanding of trends and contribute to the formulation of sound policies and strategies for fostering agricultural and other rural enterprises. Although the problems related to rural income diversification faced by more developed countries in Central Europe might be broadly similar to those of the poorest countries in the region, the differences in the underlying constraints require different approaches. Given the widely recognized importance of the role of rural income diversification strategies as an approach for improved livelihoods and poverty alleviation, the paper presents the context, concepts and terminologies in relation to income diversification and sustainable development in rural areas and provides indications on the role of FAO taking into account past and ongoing FAO activities in the region, as well as its specific expertise and comparative advantages for future assistance.

II. CONTEXT AND APPROACHES TO AGRICULTURAL AND RURAL INCOME DIVERSIFICATION

6. There has been an increasing recognition recently that the rural economy is not confined to the agricultural sector, but embraces the broad spectrum of needs of all rural people including social service provision, economic activities, infrastructure and natural resources in rural areas. Evidence from the developing world suggests that economic diversity in the countryside has the potential to foster local economic growth and alleviate the rural–urban income gap and rural poverty. The positive effect of diversification of economic activities on the income of rural households and the alleviation of employment problems of people living in rural areas is unquestionable. The importance of the concept has been increasingly emphasized in the past few years for rural development policy.

7. The context and driving forces for commercialization and diversification in developing the region's low-income food-deficit countries (LIFDCs) differ from those in the transition and developed countries. The shift from food-first strategies with systemic price risk at the local level, forces farmers to look at market options for “high value commodities” to generate cash incomes to meet food and non-food needs through introduction of market-oriented farm enterprises. In the context of Western Europe, diversification mainly relates to non-farm activities or the maintenance of a diversified enterprise mix as risk management strategy and in response to loss of employment opportunities in primary production.

8. In Europe, family farming is an important tradition. Many farms have been owned and run by the same family for generations. Corporate farming (where the farm i.e. the land, buildings, machinery and livestock is owned by a commercial company that employs a manager to run it) is rather unusual in Europe. In the new member countries of Central and Eastern Europe, agriculture is now also firmly dominated by individual ownership of both farm assets and land. The level of diversification is still relatively small and arguably enterprise diversification by farmers is unlikely to generate sufficient new jobs to solve the problem of high rural unemployment.

9. Evidence from several Central European European Union Member States indicates that diversification contributes to the increase of household incomes in a period of stagnating farming revenues. However, there are substantial deviations from country to country across the European Union and large differences in the performance of individual farms. There is growing evidence that rural households throughout Central and Eastern Europe are increasingly dependent on non-farm sources for 30-35 percent of their income and although 60 percent of rural inhabitants in rural areas are connected to a farm, only 20 percent count farming as their main occupation.

10. The importance of diversification has been increasingly emphasized in the past few years in the European Union Rural Development Policy. One of the essential rules governing the Rural Development Policy for the period 2007 to 2013, is to improve the quality of life in rural areas and encouraging diversification of the rural economy. The European Union intends that the resources devoted to the fields of diversification of the rural economy and quality of life in rural areas under this axis contribute to the overarching priority of the creation of employment opportunities and conditions for growth.

11. High level of vertical and spatial integration into agrohholdings in some Eastern European and Central Asian countries resulted in reduction of production diversification in their individual members, thus providing the opportunity to increase profitability and economic efficiency. However, based on empirical research carried out to date, there is no evidence that this became widely evident. The establishment of super-large farms had serious impact on employment and livelihoods in rural areas. In many cases farm restructuring resulted in large layoffs of farm workers, who left without alternative employment opportunities, farming their small household plots.

12. Natural resources in some parts of the region have been exploited in an unsustainable manner for decades. Agriculture was characterized by heavy mechanization, intensive use of fertilizers and pesticides, frequent reliance on monocropping, poor water management and unsustainable animal populations. On top of that, agricultural production is frequently affected by unpredictable adverse meteorological conditions, varying from regional floods and draughts to considerable losses caused by hail resulting in devastating impact on agricultural production, food security and livelihoods, and causing disruption in agrifood chains.

13. Given the globalization of agrifood value chains the competitiveness remains a key determinant in sustainable use of productive functions of agriculture. However, not all forms of agriculture are capable of reaching the same levels of competitiveness. Increasingly consideration is being given to remuneration of the non-productive functions which could permit the viability and sustainability of a less productive agriculture and increase overall rural incomes.

14. Diversification has become more important in recent years because of the uncertainties surrounding traditional farming practices (mainly associated with food production). Such uncertainties have included the fall in incomes partly because of the behaviour of markets caused by globalization and trade liberalization, as well as reform of government support policies which are increasingly removing or reducing many of the support measures that farmers, particularly in the European Union, once enjoyed. In the context of recent food price volatilities, global economic and financial crisis as well as climate change, diversification is becoming increasingly important as a risk reduction strategy.

15. Diversification can involve on- and off-farm activities and involves branching out into other activities and business enterprises either related to farming or entirely different from farming but making use of the assets that a farm typically might possess. As such, one can distinguish between enterprise and income diversification. Enterprise diversification activity embraces both on- and off-farm business creation outside of agricultural core activities. Income diversification will embrace these two components plus any movement towards non-farm employment (whether agriculturally based or not).

16. For example, agrotourism, on-farm processing, direct selling, provision of specific services, such as recreation and therapy, but also non-conventional value adding based on voluntary food standards and specific quality production schemes (e.g. organic farming, Protected Geographical Indication [PGI] or Protected Denomination of Origin [PDO]), high-value crop production, etc., constitute the most well-known *on-farm diversification strategies*. Besides value adding and increasing farm household income, new activities provide labour for a major number of the household members. The main external factors affecting farm-based diversification are related to the development of local economy and local labour markets, as well as the state of infrastructure, particularly transport and telecommunications.

17. *Off-farm diversification* in the local rural economy, or by migrating is including all those activities that are not agricultural but located in rural areas and which generate income to rural households either through wage labour or self-employment (i.e. diversification away from agriculture sector). Generally, across Europe, income from non-farm activities is rising but invariably, moving into a different business area creates significant problems; the sort of skills needed to deal with the bureaucracy, marketing and face-to-face customer service may be very different to the sorts of skills many farmers already have and many activities take away time from the main farming activities. New activities require investment in both financial terms and in learning how to manage a different business area.

18. There are numerous socio-economic pressures at the household level which act as drivers of diversification. Usually, small farms are associated with *distress-push diversification*. Those who are pushed, normally accept returns on assets or a wage below their returns to farming or their agricultural wage, as they are simply trying to increase their total household income. These households are constrained with regard to their job opportunities by their education levels,

appropriateness of skills, lack of infrastructure, etc. This suggests that the resource poor households may be pushed to diversify by financial necessity. On the other hand, more progressive, better off and larger farms generate more agricultural income and frequently have surplus assets to deploy in diversified activities, such as machinery and buildings. Providing an income generating opportunity exists, they become pluriactive. This is a *demand-pull diversification*.

19. Farms and households driven into demand-pull diversification of their income generation portfolio, in response to an observed market gap or entrepreneurial reasons are more likely to have access to higher entry barrier activities that allow accumulation. On this basis, it might be expected that pluriactive households would tend to be those within the groups of the smallest and largest farms. This is indicative of where policies should be targeted if increased and diversified incomes in rural areas are to be achieved, at the smallest and largest farm groups by providing appropriate support and creation of an enabling environment for rural business development.

III. ISSUES AND CHALLENGES

20. There is substantial scope for agricultural and non-agricultural growth in the region for sustainable poverty reduction and increased livelihood security for rural households. The challenge is to provide an enabling environment involving public-private partnerships, building of local linkages and institutions supporting innovation and investments to support diverse livelihoods, as well as improved knowledge and skills for market-oriented agriculture and preserving and improving the natural resources.

21. Changes in technology, urbanization, distribution and consumer demand for higher quality and safer agrofood products have impinged on traditional production and distribution, posing also new challenges. The agrofood value chain now requires more planning and coordination, and in particular, improved linkages between farmers, agribusinesses, retailers and consumers. Changes in consumer behaviour and increased awareness of environmental, social and economic benefits of maintaining vibrant rural areas make rural development approaches based on income diversification the main tool for future economic development policies affecting rural areas. However, there is a number of issues, bottlenecks and challenges that need to be addressed in order that these policies are effective and efficient.

22. The following section discusses some of the aforementioned identified key constraints and issues for developing rural income diversification. Factors that hinder rural households to improve their livelihoods through income diversification in a sustainable way are numerous and require the addressing of a number of fundamental challenges, such as a) human capital (e.g. know-how, expertise); b) financial capital (rural finance, markets); c) social capital (social cohesion, cooperation); d) natural capital (natural resources and heritage); and e) physical capital (rural infrastructure, investments and farm assets).

23. **Human capital and skills development** will be crucial to exploiting opportunities for growth and employment in rural areas. Developing a proactive approach to training and retraining farmers, particularly as regards transferable skills and promoting knowledge and improving human potential will be important to effectively enable the management of structural change. Training programmes need to be developed and implemented which do not necessarily form part of normal education programmes or systems at secondary or higher levels. A set of measures needs to be developed for increasing management capacities, and training on information and diffusion of knowledge, including expertise in new information technologies (IT). Furthermore, farmers and forest holders have to be encouraged to make increased use of advisory services in order to improve their knowledge and awareness in the fields of product quality, but also sustainable management of natural resources. This includes in particular, cross-compliance, the application of production practices compatible with the maintenance and enhancement of the landscape, the protection of the environment and animal welfare, which are crucial requirements for receiving European Union support.

24. A second area is the appropriate consideration of gender related issues, such as the support to young farmers of both sexes to take up and increase their entrepreneurial farming activity, linked to programmes for early retirement and land consolidation. In addition the entry of young people and women in the rural labour market needs to be fostered. The national advisory services and the rural development networks that are being established, in particular in the European Union and accession countries, have a crucial role in providing support to human capital formation.

25. However, in order that the human capital can unfold its skills, there is a need to improve the **access to financial capital**, by fostering rural finance through small- and medium-credit facilities and grant and co-financing programmes for specific measures supporting rural income diversification. In addition, the access to markets, domestic or international, is crucial for success and measures need to be devised that address this issue along the entire commodity chain.

26. One of the factors that can greatly improve the access of rural farming households to human and financial capital is fostering its **social capital**, by increasing social cohesion and cooperation among the members of rural communities, including ensuring appropriate legal frameworks. It is also important to highlight proper governance over the use of natural resources through the design and implementation of policies that create an enabling environment to enterprise and income diversification (e.g. decreasing of monocropping practices). There is a number of approaches and initiatives in this regard addressing social cohesion at different levels. For example, the establishment of producer groups, farmers' association or cooperatives¹ improves the building up of local linkages between farmers, agribusinesses, retailers and consumers along the commodity chain. At a higher level, including also local governance, administration and the private sector, as part of an integrated, bottom-up approach, the building of local initiatives, for example the so-called Local Action Groups (LAG) under the LEADER approach in the European Union, will play an essential role in connecting people to new ideas and approaches, encouraging innovation and entrepreneurship, and should promote inclusiveness and the provision of local services.

27. Also building local partnership capacity and Public Private Partnerships (PPP) will become increasingly important. At the highest level, national administration, legislation and policy-making, there is a need to build the necessary institutions that will support innovation, improved knowledge and skills for market-oriented agriculture (e.g. advisory services, vocational and life-long learning, etc.), investments for creating diverse livelihoods (e.g. national rural development support programmes² and policies), and improved and effective legislation fostering competition, protecting contracts and property rights and preventing corruption.

28. A crucial ingredient for successful rural livelihoods diversification is the efficient use and preservation of the available **natural capital**, natural resources, cultural heritage, natural and human-induced landscape, etc. These are the basics for providing modern services for enjoying rural amenities through sports activities and rural tourism, including preserving traditional crafts related to agriculture, and improving knowledge for protecting and maintaining the natural landscape. There is a need to fully recognize the intrinsic value of natural or human-induced landscapes and its role for adding value to rural economic activities. Besides this "intrinsic" valuation of natural resources, their classic use as a basis for agricultural production and forestry, e.g. renewable energy from biomass, non-wood forest products, etc., should not be neglected.

29. Globalization and market integration is also leading to a process of structural changes in the farming sector affecting the use of land. Land consolidation has proven to be an important

¹ Referring to the Western European countries widespread model of service cooperatives for trade in inputs and commodities, processing, rural finance, advisory services, etc.

² In the European Union and candidate countries substantial funding is available under the European Agricultural Rural Development Fund (EARDF) and Instrument for Pre-Accession Assistance for Rural Development (IPARD) programmes.

instrument of rural development in Europe. It is enabling farmers to become more competitive by removing fragmentation of parcels, and by allowing them to expand the size of their holdings. Land consolidation is also used to benefit rural communities by including components to improve the natural environment and local infrastructure. At the national level, land consolidation can assist with the development of agricultural and other sectors that comprise the rural and regional economy, and with improving rural conditions through balancing the interests of agriculture, transportation, environment, recreation, cultural heritage and tourism.

30. Infrastructure, investment and farm assets belong to the last of the challenges, **physical capital**, that rural households are facing. The availability of an appropriate rural infrastructure will allow farmers to benefit and value the potential income opportunities. Transport networks, telecommunications, markets, but also social and health services, administrative services and rural finance are crucial infrastructures that need to be in place. But also farms and rural households need to be able to invest and improve their productive assets in order to cope with the new challenges of globalization and market integration that demand products that are traceable, safe and produced under hygienic conditions, and follow certain specific standards and procedures. These standards can be of an administrative (e.g. food safety standards, animal welfare, etc.) or private (e.g. production standards under organic or specific quality production schemes like PGI or PDO, etc.) nature.

31. Finally, increased awareness of environmental, social and economic benefits of maintaining vibrant rural areas is the basis for devising any policy for rural households' livelihood diversification.

IV. FAO'S ROLE AND POTENTIAL TO SUPPORT DIVERSIFICATION PROCESSES IN EUROPE AND CENTRAL ASIA

32. FAO is well known for assisting its member countries in the formulation, implementation and monitoring of rural and agricultural development strategies and programmes, with special focus on sustainable use of natural resources, diversification and competitiveness improvement. Efforts are made to lower vulnerability itself through measures such as diversification of agricultural production systems, introduction of drought and pest resistant varieties, improvements in information systems and markets, and promotion of greater and more competitive access of commodities from these countries to world markets. These and other concrete activities related to more efficient and sustainable use of resources and diversification of production patterns are integrated in a comprehensive approach, to support small farmers in increasing their incomes and improving rural livelihoods.

33. In light of current global issues such as population growth and climate change, providing an adequate supply of food of requisite quality will depend on more efficient and resilient production systems using good farming practices that make efficient use of the natural resources base, coupled with an enabling policy and institutional framework. Sustainable livelihood, food safety and value-chain approaches need to underpin the increase in productivity and diversification. To address these challenges, the FAO *Strategic Objective A – Sustainable Intensification of Crop Production* promotes crop production intensification aiming at strengthening livelihoods using the benefits of increased productivity and diversification within the value chain. This will be achieved through *Organizational Result A1 - Policies and strategies on sustainable crop production intensification and diversification* at national and regional levels by policy advice and assessment of potential for sustainable market driven crop diversification.

34. Effective participation of developing country producers, especially small producers, in markets is limited and the efficient functioning of markets is constrained by *inter alia* inappropriate policies, lack of information, inadequate infrastructure, weak institutions and market power asymmetries. At the same time, employment creation in agriculture or through rural

enterprise and agribusiness development needs to be accompanied by policies that ensure fair and safe conditions in rural areas. To this effect the FAO *Strategic Objective G – Enabling Environment for Markets to Improve Livelihoods and Rural Development* through *Organizational Result G2 - Rural employment creation, access to land and income diversification are integrated into agricultural and rural development policies, programmes and partnerships*. The focus is on providing policy advice and capacity building for rural development programmes, policies and implementation, focusing on rural employment creation through farm income diversification, including relevant analytical work on rural households' sources of income, and patterns and trends in on- and off-farm employment, land tenure and access to land in agricultural and non-agricultural rural sectors.

35. Furthermore, the FAO Regional Office for Europe and Central Asia (REU) contributes to the aforementioned Strategic Objectives focusing on the promotion of enterprise development, enhancement of food quality and safety, quantitative measurement of value added, promotion of coordinated linkages among producers, processors and retailers as well as on the improvement of the competitive position of individual farms in the market place, through capacity building of value chain actors and supporters. The main thrusts of the programme in the region are promotion and capacity building for agribusiness and agro-industry development, farm commercialization and income diversification for improvement of small- and medium-sized farm income, employment and livelihoods, through the organization of regional workshops and policy consultations, publications as well as technical support to field projects related to value chain and institutional development for policy analysis and improved farmer-market linkages. This kind of assistance effectively empowers rural households in the region and fosters their position in the rural economy, markets and value chains, while contributing to the overarching objective of assuring sustainable agricultural and rural development.

36. FAO is cooperating and concluding partnerships with numerous organizations in the region, such as with the different UN organizations under the “Delivering as One” framework, the World Bank, bilateral donors and other intergovernmental organizations at subregional level.

37. FAO’s comparative advantage lays in the fact that it can combine all the technical areas into a coherent programme in partnerships that foster diversification, with the aim to improve quality of life, create employment and contribute to social equity, thus reducing vulnerability and poverty and increase food security of rural populations at all levels.

A. SELECTED FAO ACTIVITIES AND INITIATIVES SUPPORTING INCOME DIVERSIFICATION IN THE REGION

Central Asian Agricultural and Rural Development Policy Forum: Income Diversification for Sustainable Agricultural Growth

38. The goal of this first agricultural and rural development policy forum for Central Asian countries was to stimulate discussion on issues of common interest to agricultural policy-makers. This forum was based on the proposition that improved dialogue between government representatives and other stakeholders specializing in agriculture and rural development can over time lead to a better appreciation of the commonalities of policy issues pertinent to agricultural and rural development and may contribute to the search of governments in the region for solutions to these issues.

39. The topic of this first policy forum was income diversification for sustainable agricultural growth. The forum covered four main policy topics of relevance to income diversification for agricultural growth in Central Asian agrarian reform, livestock and pasture policy, crop diversification and potential of bioenergy to diversify rural incomes.

Support to Standing Working Group on Regional Rural Development for Southeastern Europe

40. The model for the agricultural and rural development policy forum for Central Asian countries is the successful *Agricultural Policy Forum for South-Eastern Europe (APF)*, which has met since 2001 on a yearly basis, hosted by a different country. The participants are Ministers for Agriculture, their deputies or State Secretaries and high-level civil servants. The APF started out as an agriculture policy discussion forum in 2001, created to build trust and improve the policy dialogue between governments of the Southeastern European countries. This initial base of trust building gradually led to the decision by the region's governments to create in 2005 a technical working group, the so-called Standing Working Group on Regional Rural Development for South Eastern Europe (SWG), and to institutionalize it as a force for collaborative improvement of the policy environment for agriculture and rural development in Southeastern Europe. The SWG is today a recognized intergovernmental body for discussion and advice on agricultural and rural development issues in the countries of Southeast Europe, with considerable policy weight and experience. The body oversees a sizeable portfolio of regional donor funded projects on agriculture and rural development designed to improve the policy environment for rural development in the countries of Southeastern Europe. FAO has been collaborating with and supporting the SWG since its inception in 2005 through different project activities and capacity building workshops, such as the recently completed regional project for "*Support to capacity building for agriculture and rural development policy analysis and formulation to support EU-integration of SEE countries*", selected as one of the success projects for the FAO Web site.

Rural Development Strategy for Medjmurje County, Republic of Croatia

41. FAO supported the preparation of the Medjmurje County Rural Development Strategy in Croatia, covering agriculture, agribusiness and rural tourism. The overall objective of the strategy is to improve quality of life and effectiveness in use of natural resource and human capital in rural areas of Medjmurje County through: (i) sustainable development of agriculture and tourism with emphasis on improvement in quality of local products and services; (ii) improved human resource base and institutional capacity for participation in and contribution to rural development; and (iii) preservation of natural and cultural heritage of rural areas in Medjmurje. These Strategic Objectives will be achieved by encouraging the development and synergies between agriculture and rural tourism as the main drivers of Medjmurje's rural development.

42. In collaboration and under the umbrella of "Delivering as One", FAO addresses the issue of income diversification also in two UN Joint Programmes funded by the Spanish MDG Achievement Fund in Serbia and Turkey.

Growth with Decent Work for All: A Youth Employment Programme in Antalya, Turkey, implemented in partnership with the United Nations Development Programme (UNDP), the International Labour Organization (ILO) and the International Organization for Migration (IOM)

43. Decent work is central to efforts to reduce poverty, and is a means for achieving equitable, inclusive and sustainable development. It involves all workers, women and men, benefiting from fundamental principles and rights at work; having access to equal employment and income opportunities; social protection and social security; and social dialogue which reflect the concerns of governments, workers and employers.

44. The overall objective of the Joint Programme (JP) is adoption and implementation of employment policies benefiting the most vulnerable groups in the labour market within the context of Turkey's east-west migration. The JP aims to reduce youth unemployment and increase the participation of young women in the labour force. This will be achieved through improved capacities at national and local levels to design and implement employment interventions for vulnerable communities and young women. A National Youth Employment Action Plan will lay the policy, budgetary and institutional framework for this objective. In addition, new labour-

intensive employment opportunities for young men and women will be enhanced through vocational training.

Sustainable Tourism for Rural Development, Serbia, implemented in partnership with the United Nations Environment Programme (UNEP), UNDP, the United Nations World Tourism Organization (UNWTO) and the United Nations Children's Fund (UNICEF)

45. Sustainable rural tourism is one of the key sectors with strong potential for diversifying Serbia's rural economy. In the past several years a movement has been developing toward sustainable rural tourism that counters the threats of unmanaged tourism. In short, it minimizes environmental and cultural damage, optimizes visitor satisfaction, maximizes long-term economic growth and balances tourism growth potential and the conservation needs of the environment.

46. The JP has two key outcomes that will be achieved through a holistic approach of UN agency and partner cooperation: (i) legal and policy framework for supporting diversification of rural economy through tourism will be developed to achieve the Millennium Development Goals; (ii) local rural tourism and support industries will be better linked and organized; and local stakeholders' capacity will be improved for delivering services and products in line with national strategies. A Joint UN Fund for Sustainable Rural Tourism will provide investments in three thematic windows: i) tourist destination development; ii) diversification of rural economy through tourism; and iii) active learning tourism investments.

V. OPTIONS AND AREAS OF INTERVENTION TO FOSTER INCOME DIVERSIFICATION IN RURAL AREAS

47. Increasingly, market forces and trade liberalization are impacting significantly on rural livelihoods. Whilst these changes lead to new opportunities they can also increase the vulnerability of smallholder farmers and rural entrepreneurs to market pressures. Diversification into market-oriented income generating activities and participation in market economies is unavoidable if rural communities are to survive. The key issue is how to support engagement in the market in a way that promotes equitable and sustainable growth in the local rural environment.

48. Given the globalization that the agriculture and rural economies are exposed to, it is assumed that stakeholders (i.e. rural households) need to be informed of developments in international markets, trade policies and rules, food safety, hygiene standards and other private quality standards and schemes, in order to have the capacity to exploit market opportunities. A non-exhaustive set of possible options and areas of intervention is presented for consideration and discussion.

49. Further integration can be expected in the agrifood value chains. Increasing emphasis will need to be placed on further developing and strengthening buyer/producer linkages and in the development of supply contracts. To gain competitive advantage in the global marketplace, and to create and market new products and develop new outlet key ingredients will be high quality, planning and evaluation, perseverance, focus and building long-term relationships with customers. Measures need to be in place aimed at improving the quality of agricultural production to help farmers to adapt to demanding standards and to support farmers who participate in food quality schemes.

50. Cooperation between producers and between producers and other stakeholders in a value chain should assist in the development of new products, processes and technologies and in particular to determine and monitor common rules and standards as well as to inform consumers and promote products provided under quality schemes.

51. Evidence from a number of countries indicates that diversification contributes to increase of household incomes in a period of stagnating farming revenues. The main external factors affecting farm-based diversification are related to the development of the local economy and the

local labour market, as well as the state of infrastructure, particularly transport and telecommunications. Education levels, age, capital availability, social capital and networks and farmers' perception and preferences are the most important internal factors that need to be strengthened to enable successful diversification.

52. Vocational training and information actions also need to assist in the diffusion of scientific knowledge and innovative practises for persons engaged in the agricultural, food and forestry sectors. Innovation will increasingly become important for Europe's farming, agrifood and forestry sectors. While Europe's large agrifood companies are often at the cutting edge of new trends, the introduction of new products and processes could significantly contribute to the performance of smaller processors and farm businesses.

53. From the farmers' point of view, based on CAP experience, policies inhibiting diversification include stabilization of prices of farm outputs, direct payments, investment subsidies, tax exemptions and subsidies to farming credit. Policies and initiatives for encouraging diversification include provision of seed money for business start-up, loan guarantees, tax exemptions for diversified enterprises, advice on completing loan or grant application forms, business training and advice on business planning, as well as non-pecuniary benefits like free health care and training to undertake off-farm employment.

54. Diversification is the main tool that farmers have to reduce their individual farm risk. Although frequently easily suggested as an option farm diversification is not always easy to achieve as there are often no clear profitable options and the financial costs of changing/adding enterprises are high. Well researched farm diversification strategies are needed to guard against price shocks.

55. There is also a further need to encourage the further take-up and diffusion of information and communications technologies (ICT). The agrifood sector as a whole has been identified as lagging behind in the take-up of ICT technologies. This is particularly the case for smaller businesses. The take-up and diffusion of ICT is essential in rural areas for diversification, as well as for local development, the provision of local services and the promotion of e-inclusion. Economies of scale can be achieved through village ICT initiatives combining IT equipment, networking and e-skills training through community structures. Such initiatives can greatly facilitate IT take-up by local farms and rural businesses and the adoption of e-business and e-commerce. Full advantage needs to be taken of the possibilities afforded by the internet and broadband communications to overcome the disadvantages of remote locations.

56. The desire to increase income by taking advantage of market opportunities requires farmers to become better decision-makers and better at competing in this new environment. Although there are numerous programmes and support initiatives to offset diseconomies of scale and improve farmers' bargaining power and position in a food chain, due to the inappropriate extension and consulting services, knowledge about potentials and benefits of cooperation, commercialization and diversification is still limited. Advisory services need to be adapted accordingly and to provide specific and relevant advice. The use of business development and advisory services should allow them to improve sustainable management of their holdings.

57. Experience has shown that commercialization and vertical integration in the food chain may be solutions only for a limited number of well organized and equipped farms with credit standing or informal borrowing capacity and skilled management. Lack of start-up capital combined with non-transparency of operational procedures inhibits smaller farmers to commercialize. Possible solutions for those could be alliances with other farmers or contract arrangements with agribusiness.

58. There is also a particular need to encourage investment into technology-based businesses with high growth potential, small businesses, start-ups and spin-outs and clean environmental technologies. Improvements in the processing and marketing of primary agricultural and forestry products should be encouraged by means of support for investments aimed at improving

efficiency in the processing and marketing sector, introducing new technologies and innovation, placing emphasis on quality, improving environmental protection, occupational safety, hygiene and animal welfare, as appropriate, by targeting, as a general rule, micro-, small- and medium-sized enterprises.

59. To a varying degree, much of rural infrastructure still needs to be upgraded throughout rural areas of the region. Significant investments will need to be made in telecommunications, transport, energy and water infrastructure, as well as rural market infrastructure over the coming years. There is broad recognition that rural infrastructure development cannot be seen as solely a government responsibility. As a result of structural adjustment and privatization the public sector has increasingly withdrawn from the construction, management and financing of rural infrastructure works and the private sector has been encouraged to step in. To address today's infrastructure challenges there is a need to look beyond simple solutions and take into account the following: that the private sector is unavoidable; domestic capital needs to be tapped; that there is a need to improve cost recovery; that there is a need to better understand the legal traditions of a country in order to better design PPP arrangements; and that there is a need to improve governance and accountability through institutional designs.

60. The role of diversification in sustainable use and management of natural resources is unquestionable. For example, agricultural land needs to be protected and its structure improved. Spatial or physical planning, land use planning or urban planning will influence the availability of quality agricultural land for farming. Furthermore, the issues affecting land tenure and land consolidation need also to be addressed in order to maintain the agricultural base of rural areas, and to provide income and opportunities for livelihoods diversification. Land consolidation will need to be applied differently in different situations. But regardless of the context in which land consolidation is applied, it can be used to introduce integrated, participatory and cross-sector approaches into rural development.

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