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ASSESSING THE RESEARCH FRAMEWORK AND INSTITUTIONAL CONTEXT FOR RURAL DEVELOPMENT POLICY: DISCUSSION

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David McGranahan has done a thorough job of examining economic conditions in rural areas. Because I have little to add to his assessment of the rural economy, I will focus on the changing institutional context of rural development policy.

The institutional context in which rural development policy will be made in the 1990s is shaped by at least four factors that deserve our attention: (1) changes in intergovernmental relations that are redefining the responsibilities of the federal, state, and local governments, (2) a high degree of obsolescence in many of the public institutions that govern local rural economies, (3) high transaction costs that make the development and implementation of rural development policies problematic at best, and (4) the internationalization of the economy.

Intergovernmental relations are changing rapidly in the U.S. and, in some cases, to the disadvantage of rural areas. The federal government, the states, and local governments are redefining their relationships and changing the responsibilities and resources of each level of government (Stanfield). This sorting-out process has two components. First, the burden of the cost of public services is shifting among the three levels of government. Second, the increasing number of mandates imposed by higher levels of government on lower level jurisdictions is creating an environment in which higher level decisions determine an increasing proportion of lower level budgets.

The first component is evident when examining the declining federal resources provided to state and local governments. Federal grants to state and local governments for community and regional development programs declined by nearly 30 percent in nominal terms between 1978 and 1990, and the President's FY 1992 budget recommended an additional 20 percent reduction by Fiscal Year 1996. Even worse for local rural governments, 83 percent of this funding is expected to be devoted to programs under the jurisdiction of the Department of Housing and Urban Development, leaving very little funding for economic development in rural areas (Office of Management and Budget 1991b). As a result, state and local governments are bearing an increasing share of the cost of public services in rural areas, even in those cases where a reasonable argument can be made for federal cost-sharing. For example, the share of state and local expenditures on physical capital financed by federal grants declined from 36 percent in 1980 to 23 percent in 1990, the lowest federal share since 1960 (Office of Management and Budget 1991a).

These trends are exacerbated by the rising number of legislative mandates dictating that lower level jurisdictions of government provide an array of regulatory and social service programs without providing the means of financing such programs. As Martha Derthick has observed, the constraints imposed by the lingering federal budget deficit are creating a misalignment of jurisdictional responsibilities and resources:

> In particular, there is a danger that Congress, in striving to close the gap between its desire to define large goals and its unwillingness to provide the administrative means to achieve them, will try to conscript the states. That is, it will give orders to them as if they were administrative agents of the national government, while expecting state officials and electorates to bear whatever costs ensue (quoted in Conlan, p. 54).

This trend—which is now spreading as the states impose more mandates on local governments—threatens to crowd out the legitimate expression of local preferences as an increasing share of state and local budgets are dictated by higher levels of government (Stanfield; Conlan). This trend also imposes a rising administrative burden on local governments that are already struggling under a lack of adequate human resources for administrative functions. The net result of these two trends—a shift in the cost of public services and the rising number of intergovernmental mandates—is that the federal grant system is increasingly determined as a residual of larger policy

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decisions (e.g., deficit reduction or macroeconomic stabilization), often with little concern for the impact of these decisions on state and local governments. As a result, our intergovermental grant system is losing the logic and rationalization necessary to truly be called an integrated public finance system (Haughwont and Richardson).

The second element in the rural institutional context is that rural areas are increasingly plagued by public institutions that are obsolescent when measured against the needs of the 1990s. Despite the migration of population out of rural areas during the past half-century, the basic units of rural government—the county and township—have not changed. As a result, these institutions are increasingly unable to deal effectively with the administrative burden of present day problems. The current system of local governments also creates additional administrative overhead, with predominantly rural states having more state and local government employees per capita than other states. Nine of the thirteen states in the southern region have more state and local employees per capita than the national average (U.S. Department of Commerce). As Schuh (1989) has observed, reorganization of local governments is a politically sensitive issue, but "the issue is whether we can really afford to limp along with the present antiquated system." It should be noted, however, that we know very little about economies of scale in local government. Innovative research and extension programs are needed to address these difficult issues.

It should also be noted that advances in technology often require institutional changes that make the use of such technology feasible. For example, McGranahan describes the limited impact of fiber optic technology as a catalyst for rural economic growth. An equally important factor is that changes in rate structures and utility regulations are often required before the installation of fiber optic systems can be justified in many rural areas (Fulton).

The third factor affecting the institutional context of rural development policy is the high transaction costs that must be incurred in establishing effective development policies. An effective rural development policy must address the four factors that contribute to economic growth—changes in technology, changes in institutions, investments in human capital, and investments in natural and manmade capital. These factors are complementary and, while all of them are necessary, each alone is insufficient to accelerate economic growth (Johnson et al.). Marshalling all of these forces requires a concerted effort of state, local, and national policymakers. Consequently, the political transaction costs of coordinating such efforts present a major barrier to the development and implementation of rural development strategies that are capable of addressing the unique problems of diverse rural areas (Bonnen; Freshwater).

The difficulty of organizing an effective political effort on behalf of broad-based rural policies is heightened by the advantages held by farm organizations relative to other rural residents. Well-organized farm groups have dominated the rural policy agenda and, by promoting a mixture of agrarian and physiocratic philosophies, have established the view that commodity policies are the central element of an effective rural development policy. Rural residents who are unaffected by such policies are at a distinct disadvantage in advancing a broader policy agenda for rural development (Rasmussen).

It is now a cliche to say that we are operating in a global economy, but the rapid pace of change in world trading arrangements will continue to bear on the viability of rural economies. The development of trading blocs in Europe, North America, and perhaps in the Pacific Rim could provide opportunities for some rural areas, but will also present challenges to local business and government leaders. Proximity to these blocs could affect the ability of industries to compete in these markets, and some observers believe that states along the East Coast will gain from an expansion of the European market just as the West Coast has gained from an expansion of trade in the Pacific (Lemov). At the same time, states and localities will be forced to meet the harmonized regulatory standards of the European Community and to develop business, tax, and banking regulations that are attractive to European investors if they are to compete in the EC. To add further complexity to this problem, we are having an ongoing debate over the rights of state governments to establish business regulations versus the right of the federal government to preempt state regulations with national regulatory standards (Moore). To the extent that the states prevail in this debate, state and local governments will have to factor international compatibility into their regulatory decisions. Once again, this requires a level of expertise that is unavailable to many local governments and even some states. With states in the southern region selling 23 percent of their exports in the European Community (Lemov), these problems are relevant to the southern region.

The research framework used to analyze rural development issues must recognize the institutional context in which rural development policy is made, if our research efforts are to produce useful results for policymakers and rural citizens. This framework must emphasize intergovernmental issues and integrate dimensions of public finance theory, public

choice and transaction cost economics, and international trade theory. In addition, we must begin to examine the policy implementation process. Greater emphasis must also be placed on redesigning institutions (Schuh 1992) and on the distributional impacts of the non-Pareto optimal policy choices that must be made (Johnson et al.). This is a demanding agenda, but progress can yield improvements in rural life and bring credit to our profession.

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