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Asset-Building in Rural Areas

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Abstract

Rural areas have low population densities. On the one hand, this develops social capital and entrepreneurship and permits agriculture. On the other hand, it increases the costs of transactions and providing public services. This makes asset-building more difficult in rural areas. For example, it costs more per capita to provide schools, roads, and hospitals, people are more likely to work in small firms that do not offer access to asset-building institutions such as group health insurance or 401(k) plans, and rural homes are less likely to appreciate in value. From a policy perspective, access to asset-building institutions could be decoupled from employment at a large firm. Policy could also enhance existing rural assets by improving the staples of any socio-economic system: schools, roads, safety, parks, and the environment.

Asset-Building in Rural Areas

1. Introduction

How does ruralness affect asset-building? Rural areas are defined by an abundance of natural resources relative to people. In general, this low population density constrains asset-building by increasing distances and thus increasing transaction costs, that is, the costs of transport, communication, decision-making, and coordination. Low population density also increases per-capita costs for the provision of public goods such as schools, roads, and hospitals. In general, rural areas lack "economies of agglomeration" (Krugman, 1995).

At the same time, low population density creates asset-building opportunities:

- Repeated contact with the same few people helps build social capital which may then reduce coordination costs in the provision of public goods
- New types of resource extraction (such as the provision of waste sinks and the enjoyment of natural amenities) complements traditional agriculture and mining, in some cases without degrading the environment
- The seasonality of rural job opportunities, the general fragmentation of markets due to transaction costs, and the lack of inexpensive alternatives to "doing-it-yourself" build human capital and encourage entrepreneurship
- Rural areas promise an alternative lifestyle for people tired or scared of modern urban life

The only way forward is to use existing assets to generate more resources for saving and investment to take advantage of changes in the economic and social landscape. At the same time, rural areas must also improve the provision of public goods so as to reduce transaction costs.

Because assets beget assets, both approaches can spark virtuous circles, but the key is to focus on the most effective investments.

Other than higher transaction costs, the task of asset-building is basically the same for both rural and urban households; they must consume less than they earn and then save the difference. The role of public policy in asset-building is also similar in both rural and urban areas; government must provide public goods—both physical and institutional—that help households build assets.

In rural areas, however, low population densities mean that governments and households must spend more for a given level of public or private goods, leaving fewer resources available to save. Saving more requires earning more and/or consuming less, attracting greater subsidies, or improving asset-building institutions. Households can always build assets by tightening their belts and working better, but this is beyond the ken of policy. Subsidies are policy-relevant, but their role in rural asset-building is a political question only briefly discussed in this paper. The most feasible, sustainable, and policy-relevant strategy is to improve asset-building institutions and to focus on classic public goods.

The next section discusses how low population densities and long distances affect rural asset-building. The sections after that look at pros and cons of specific approaches for improving rural asset-building. The final section summarizes the main points.

2. How asset building differs in rural areas

Improving rural asset-building first requires understanding asset-building in general and then understanding the unique features of rural asset-building.

3.1 A definition of asset-building

Asset-building is the accumulation of resources (Schreiner and Sherraden, forthcoming). Resources help people to do and to be what they have reason to want. Income is an inflow of resources in a period of time, while assets are resources kept through time. Consumption uses up resources. If income in a period exceeds consumption, the result is saving, an increase in resources kept through time, that is, an increase in assets. If consumption exceeds income, the result is dissaving and a decrease in assets. Asset-building occurs when, over time, saving exceeds dissaving.

Income and saving, while distinct, are nevertheless tightly linked. Saving produces assets, and employing assets (be they human, physical, social, or financial) produces income. Thus, increasing income requires saving to build assets.

3.2 Sources of resources for asset-building

By definition, sources of resources equal uses of resources (Schreiner et al., 2001):

Sources	=	Uses
	or	
Income	=	Consumption
+ Appreciation		+ Maintenance and Depreciation
+ Debt Assumed		+ Debt Repaid
+ Gifts Received		+ Gifts Given
+ Subsidies Received		+ Taxes Paid
+ Savings Added		+ Savings Used

In a given period, net saving is the difference between sources and uses:

Net Saving	=	Sources – Uses
	or	
Net Saving	=	Income – Consumption + Net Appreciation + Change in Debt + Net Gifts + Net Subsidies

Increases in net saving (and thus in asset-building) come from increases in income, decreases in consumption, increases in net appreciation, changes in debt, increases in net gifts, and/or increases in net subsidies. These potential drivers of rural asset-building are considered next.

3.2.1 Increased income

For a given level of consumption, more income frees up more resources to save and thus increases asset-building. The question, of course, is how to increase income. The answer involves working harder (more hours or more effort) or working smarter (investing in human capital and other complementary assets).

Policy has limited influence on hours or effort, particularly in rural areas where many people are self-employed or work at seasonal jobs in which they must make hay while the sun shines. In any case, rural people already have a reputation as hard workers. What policy can do is facilitate investment in human capital to make a given level of work more rewarding as well as provide public goods to reduce the transaction costs associated with a given level of output. Among other things, this means improving schools, health care, and the physical environment (for greater human capital), and improving roads, security, and the communications infrastructure (for reduced transaction costs). Of course, these are the classic roles of government.

3.2.2 Decreased consumption

For a given level of income, less consumption frees up resources to save. With time, increased asset-building allows consumption levels not only to resume but also to increase. Rural people already have a reputation for frugality, perhaps developed through generations by the need to save between harvests.

Policy can ease the sacrifice of decreased consumption by making investments in human capital and by providing public goods to reduce transaction costs. Well-educated people can produce a given output with fewer resources, making more resources available for a given decrease in consumption. A reduction in transaction costs has a similar effect.

3.2.3 Net appreciation

Appreciation is an non-maintenance increase in the value of an asset, and depreciation is a decrease. Maintenance is investment to counteract depreciation.

Appreciation is especially important for rural housing, cars, and physical business assets. Most urbanites assume that home ownership is a good investment and that houses appreciate, and elderly urban home owners often view their house as insurance against the risk of outliving their other assets. Rural home owners, however, may face depreciation, for example, when homesteads are stranded by farm consolidation or when towns lose residents. The low demand for rural housing has reduced prices to the extent that, compared with poor urban households, poor rural households are twice as likely to be home owners (Katz Reid, 2004), although many of these rural households own manufactured homes that do not appreciate.

Cars depreciate (and must be maintained) in both rural and urban areas. In a few large cities, public transport may allow households to get by without a car, but long distances and the absence of public transport in rural areas make a car a necessity.

The wealthy in rural areas tend to have a large share of their assets in illiquid forms such as land, buildings (like homes, at risk of depreciation), and machinery (like cars, certain to depreciate). While land values can go up (say, due to agricultural subsidies), they can also go down (when subsidies are cut, or from climate change).

What can policy do to enhance rural asset-building via appreciation? For housing, the basic issue is weak demand due to falling population, suggesting that the advantages of rural areas as a place to live have not compensated for their disadvantages as a place to work. Also, rural residents may buy manufactured homes in spite of plentiful, inexpensive rentals so that they can more easily follow jobs. Also, a new manufactured home may cost about the same as an older, free-standing home.

To attract residents and strengthen demand for housing, governments should focus, as usual, on their classic role as providers of public goods. Excellent schools, good roads, lots of parks, perhaps a small airport, and a reputation for safety can only help attract new residents and stem the outflow of young, highly skilled workers (Pezzini, 2000). Businesses that might move to rural areas would also consider these amenities as implicit compensation for their employees. Of course, the effect on appreciation is only one of many reasons for policy to focus on the provision of the standard set of public goods that are of greatest concern to most households.

Policy cannot do much to help agriculture diversify out of its illiquid assets (Wiggins and Proctor, 2000; Hite, 1997), and it may be some time before rural public transport is again practical.

3.2.4 Change in debt

In principle, it makes sense for households and governments to borrow for projects whose returns cover repayment plus interest. In the long term, of course, debts must be repaid. While lenders and personal liability constrain household borrowing, political incentives and diffuse liability encourage governments to borrow now—regardless of returns—and leave repayment to future administrations or generations. Few public investments (other than traditional ones such as education, health care, transport infrastructure, and agricultural research and extension) have a track record to justify borrowing.

Federal policy has traditionally supported rural areas in general and agriculture in particular via subsidized loans, arguing not only that they increase profits for farmers but also that farming, with its low margins and long gestations, cannot bear market rates. In practice, however, subsidized loans have distorted markets, benefitted wealthy landowners, and in general run counter to inclusive asset-building (Jensen, 2000; Gale, 1991; Adams, Graham, and Von Pischke, 1984). The recent wave of bank mergers has not hurt access to credit (Featherstone, 1996; Neff and Ellinger, 1996).

3.2.5 Net gifts

Rural households may sometimes receive remittances from non-resident family members. (Such remittances are more common abroad than in the United States.) Such gifts, however, usually support consumption by the elderly. Furthermore, policy cannot affect them much, except to the extent that remitters send more when they plan to move back someday, which is more likely for areas with good public services.

3.2.6 Net subsidies

Certain subsidies and taxes are particularly relevant in rural areas. Agricultural subsidies aim to support rural economies, strengthen small farms, and allay fears that, if exposed to the free market, all farmers would go bankrupt. They also result from lobbying by small, wealthy groups of landowners (for example, through state farm bureaux) and from urbanites who long for a pastoral ideal, fear food shortages or international interdependence, or still have family on the farm.

Inheritance taxes matter more for farmers than for others because, as small businesses, farmers may have a lot of assets to bequeath. Farmers oppose these taxes not only because they would rather not pay them but also because a farm may not be viable if heirs must sell part of it to pay taxes (a difficulty not faced by those who inherit less or who inherit liquid assets). Of course, inheritance taxes were not designed to affect farmers disproportionately; they do so only because farmers are so wealthy.

Agriculture (a type of resource extraction) is a pillar of the rural economy. While successful farmers do build assets, farming does not promote broad-based, inclusive asset-building. As technology advances and global markets integrate, there are fewer owners and more hired hands (Pezzini, 2000). Resource extraction by large firms (whether in agriculture or mining and whether in Africa, Latin America, or the ante-bellum South) has rarely spread wealth (Easterly and Devine, 2003). The nature of modern agriculture runs counter to the intent of the original Homestead Act (Williams, 2003) and to attempts to make asset-building more inclusive (Sherraden, forthcoming).

Overall, agriculture has no stronger claim on subsidies or tax breaks than any other industry. Long-term, sustainable, widespread asset-building in rural areas cannot rely on special tax treatment, trade barriers, or direct subsidies anymore than asset-building in the inner city can

(Porter, 1997). Hite (1997, pp. 236–8) says that investment subsidies may be the only way to help declining rural areas, but that they “will turn into a feeding frenzy of rent-seekers.” In any case, globalization and trade agreements will increasingly limit such subsidies (Pezzini, 2000). So what can policy do?

Like other rural sectors, agriculture benefits from lower transaction costs and better public goods. For example, management skill (built through education) is the key input in farm businesses. Communication and transport infrastructure remain essential for getting produce to market, managing weather and water, and minimizing trips into town. Agricultural research and extension have broad benefits for both producers and consumers (Makki, Thraen, and Tweeten, 1999). As usual, policy should focus on providing classic public goods.

This section has repetitively called for enhancing asset-building in rural areas by improving the provision of classic public goods such as education, health care, and transport. The next section offers a few concrete recommendations for improving asset-building institutions in rural areas.

3. Improving institutions

Apart from transaction costs, both rural and urban households face the same asset-building task; consume less than income and then save the difference. The role of public policy in asset-building is also similar in both rural and urban areas; provide public goods—both physical and institutional—to help households build assets.

Of course, “Improve institutions” can be a facile policy recommendation. What institutions should be improved, and how? If there are institutional improvements “lying on the sidewalk”, why haven’t they already been picked up? The answer is that low population densities can reduce the effectiveness of asset-building institutions.

For example, group health insurance and retirement savings via 401(k) plans are delivered nationwide by employers large enough to dilute the fixed costs of sponsoring these “fringe benefits”. In rural areas, however, small firms are more common, and small firms are less likely to provide access to these asset-building institutions (Besser, 1998). The policy implication is that rural asset-building would improve if access to group health insurance and 401(k) plans were decoupled from employment in a large firm. (Such decoupling would also enhance urban asset-building.)

As another example, agricultural policy—a rural-specific policy—has historically linked subsidies with land ownership. These subsidies become capitalized in the price of land and end up concentrating wealth among existing landowners (Goodwin, Mishra, and Ortalo-Magné, 2004; Floyd, 1965). If the goal is to subsidize rural asset-building, then subsidies should be linked to people (perhaps via individual accounts) rather than activities (agriculture) or existing wealth (land ownership).

A final example concerns the focus of asset-building policy at the state and local levels. “Quick fixes” (such as the stroke-of-a-pen institutional changes just presented) are tempting, but history and theory suggest that governments best support asset-building by providing public goods that decrease transaction costs and that therefore increase household income and decrease the cost of household consumption. Providing such public goods—schools, roads, public transport, hospitals, public spaces, public safety, and clean air and water—is the classic role of government. Unfortunately, these are also difficult, long-term tasks, and quick fixes may offer greater short-term political rewards. Perhaps the single-most important policy recommendation for rural asset-building is that government should focus on the basics. Providing public goods is more costly in rural areas, but the relative scarcity may also lead to higher returns.

4. Other strategies

This section discusses additional approaches to rural asset-building. While each strategy has a role in specific places, none is as applicable for rural areas in general as reducing transaction costs and improving the provision of classic public goods.

4.1 Small business

Small business ownership is not only part of the American Dream but also an economic pillar. This is particularly true for rural residents, one-third of whom are self-employed (Bailey et al., 2004), mostly in non-farm jobs. Distances help protect rural business from competition; a locally owned Tastee Freez or Tru-Valu hardware store might survive if the nearest McDonald's or Home Depot is 50 miles away.

Ruralness pushes people into entrepreneurship. Much agricultural work is seasonal, so people must patch together multiple jobs to support themselves during down times (Edgcomb and Thetford, 2004). Farmers in particular must master scores of skills, from mechanics to genetics to futures markets.

Experience creates its own comparative advantages, so entrepreneurship—even if due to necessity—is a strength of rural areas. The policy question is what to do with it. While "doing-it-yourself" builds human capital, it also inhibits economies of specialization (Sherraden, 1991). Furthermore, improvements in transportation and communications will slowly erode rural firms' protection (Wiggins and Proctor, 2000). For some people, self-employment and patching together multiple jobs means freedom and a dream come true, but most others would rather be employees.

For these reasons, policy should support an "enabling environment" for rural small enterprise without directly promoting it and without abandoning general education and job training. This means providing "more attention to quasi-public goods and 'framework conditions' which support enterprise indirectly . . . [and] improving the quality of the business environment or building social and human resource capital" (Pezzini, 2000, pp. 48, 53).

4.2 Agriculture, manufacturing, and services

Rural areas have a permanent comparative advantage in terms of land, so agriculture will always be part of their economies. But agriculture is no longer the main employer, and agricultural employment will continue to fall. Agriculture has traditionally been a way to spread wealth (for example, through the Homestead Act), but as technology increases farm sizes and the use of machinery, agriculture now concentrates wealth.

In the past, manufacturing also spread wealth, built the middle class, and was a pillar of small-town economies (USDA, 1995). The days when someone with a high-school education can work in a factory and support a middle-class family, however, are largely over, reducing opportunities for asset-building through home ownership and retirement saving for a large segment of the rural (and urban) population. Rural areas simply cannot compete with low-wage workers overseas.

That leaves services and information. Retail and food-service jobs, however, require a critical mass of population. They also pay low wages, so they are not an effective wealth-building tool for rural areas. Elder care and health care are other sources of low-paid employment in rural areas, at least for a few decades.

4.3 Attracting new residents

In a digital age in which cell phones and the internet drastically reduce some forms of transaction costs, information workers are not—at least in economic terms—tied to a specific place. Rural areas, as a good place to live, might attract them. Even if the United States is not a nation of yeoman farmers, it might have more yeoman tele-commuters. In the same way, retirees might move to rural areas because they could, in theory, live wherever they wanted.

Overall, rural areas have not attracted many retirees or tele-commuters. In social terms, retirees want to stay near friends and family, and information workers seem to prefer chatting around a water-cooler in an office rather than over the internet from home. In economic terms, information workers still need to travel frequently, and so they may be willing to move to a rural area only if they can quickly get in and out for business trips. Retirees likewise travel often for family visits, and they also seek areas close to hospitals and shopping. This suggests that building roads, developing airports, and providing mid-distance public transport might help attract new residents. Hospitals also matter, but they require a critical mass of both patients and skilled workers.

Rural areas might also use their most visible and abundant asset—land—to attract new residents. (In rural areas of poor countries, land redistribution is often the major asset-building policy.) Redistribution of private land that has been appropriated or purchased by the government, however, is unlikely, and most public lands are not attractive home sites. Thus, if retirees and tele-commuters are to buy rural homes, they must be attracted by complementary public goods such as schools, parks, and hospitals. Given their abundance of land, rural areas have a particular comparative advantage in the provision of parks and other public spaces.

In short, rural areas must become even better places to live (for those who can make a living there) by providing greater public goods in spite of the high costs.

4.4 Niche markets

Niche markets can work, but only in niches. For example, Pezzini (2000, p. 47) notes that some rural firms sell "unique products that reflect the cultural heritage of a particular region."

This strategy, however, can work only for a few people in specific places. There is not a large market for hand-quilted blankets or other arts and crafts.

Likewise, “boutique” agriculture—for example for organic produce—can work close to large cities but is not an important option elsewhere (Wiggins and Proctor, 2000). Large-scale, widespread progress in rural areas cannot rely on specialty or luxury items sold to high-income urbanites. Rather, it must focus on goods and services that account for large shares of most households’ spending.

4.5 Social capital

Rural areas are strong on social capital. Low population density increases the likelihood of repeated contact with the same people, increasing the rewards to cooperation and facilitating the development of trust as well as affection and affinity. Rural dwellers may also be more committed to being “country” (and more concerned about community well-being) than urbanites are to being “city”.

Social capital helps people cooperate. But is social capital within the ambit of policy? How (or why) should the government promote things like bowling in a league or attending high-school sports events?

Asset-building in rural areas is difficult, and reducing transaction costs and providing better public goods requires that households and governments work harder, work smarter, and/or consume less. All this requires motivation. It also requires coordination; one household, civil servant, or agency working for rural development will bear private costs that will not likely produce compensating public (or private) benefits unless many other people join in. Reversing community decline takes community commitment, and social capital facilitates this and provides a reason for hope.

So policy can use social capital; can it also help build it? One simple tool is information; governments could tell rural households that reversing decline requires extra effort to save and participation from everyone. People are more likely to cooperate if they are aware of the benefits and if they are told that they should. Local governments can establish rallying points for communities by declaring goals (and pursuing five-year plans) such as “making our schools the best in the tri-state area” or “developing an airport with a daily flight the nearest big city” or “increasing the doctors in the county by 25 percent”.

4.6 Other approaches: summary

Rural areas are diverse, and no single strategy works everywhere (USDA, 1995). Unfortunately, no one—including this author—can pretend to sit down and give birth to a new strategy for asset-building in rural areas that can hope to have more than a marginal impact. For this reason, this paper emphasizes the provision of classic public goods; they are fundamental for all households in all places, rural or urban. In fact, asset-building in rural areas is a lot like asset-building in urban areas. They both require improving public goods: developing schools; providing hospitals; maintaining parks; building roads and airports; supporting research, development, and extension; and keep the environment clean. Improving these areas is not the newest thing, nor is it simple (especially in rural areas), but it does offer high long-term returns.

At the same time, the United States and the rest of the world are rapidly moving toward a more competitive, service- and knowledge-based economy in which place means less and less. This provides a unique opportunity for rural areas to build on their comparative advantage as a place to live. Rather than chase smoke-stack industries with tax or environmental abatements, rural areas might attract paper-stack industries with top-notch public services.

5. Conclusion

By definition, rural areas have low population densities, and this affects asset-building by increasing transaction costs and the per-capita costs of public services. At the same time, low population density strengthens social capital, promotes entrepreneurship, and allows for natural-resource extraction, not only via agriculture but also via the provision of environmental, leisure, and "lifestyle" services.

Overall, rural areas are better as places to live than as places to earn a living or to build assets. Low population density increases the costs of using and providing asset-building institutions. The prevalence of small firms reduces access to employer-sponsored asset-building institutions such as group health insurance and 401(k) plans. Home ownership in rural areas does not offer the same opportunities for appreciation as in urban areas. Finally, agricultural subsidies are capitalized in land prices, concentrating land ownership and replicating a general pattern of subsidizing asset-building for those who are already wealthy (Sherraden, 1991).

Rural areas have their asset-building work cut out for them. While the internet and advances in technology will help, transaction costs will always be higher and markets will always be more fragmented. Thus, asset-building in rural areas will mean doing more with less and focusing on key areas. While rural areas face greater material challenges, they also can draw on greater stores of social capital and entrepreneurship.

What can policy do? According to Drabbenstott (2000, p. 41), “the real challenge in rural America is creating more wealth, and there is no ready formula to do that consistently.” While a national rural conference reached “no consensus on which policy approach holds the greatest promise for rural America, there was general agreement that a new path is essential” (Drabbenstott, 2000. p. 39). In other words, something must be done, but no one knows exactly what.

This paper advances a few small suggestions. At the federal level, policy could decouple access to group health insurance and 401(k) plans from employment in large firms, thereby mitigating barriers to asset-building in rural areas that are due to the prevalence of small firms. Apart from rural-specific subsidies (such as for agriculture or rural roads), however, there are few ways for policy to decrease the per-capita costs of providing public services or to increase the demand for rural housing.

At the state and local levels, rural asset-building policy should focus on improving the staples: schools, roads, safety, parks, and environment. This is more subtle, long-term, difficult, unglamorous, and expensive than introducing new strategies, but it plays to the strengths of what public policy can do (and what private action cannot), and it builds on assets that rural areas already have.

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