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Small farms in Italy: public support, diversification and economic sustainability

Małe gospodarstwa rolne we Włoszech: wsparcie publiczne, dywersyfikacja i trwałość ekonomiczna

Elisa Ascione, Roberto Henke, Francesco Vanni
Istituto Nazionale di Economia Agraria, Rome, Italy

Abstract. The paper explores the role and the significance of multifunctional activities for small farms in Italy, by analysing both farming and non-farming activities present on farms on the basis of the Italian FADN database (Farm Accountancy Data Network), covering the period from 2003 to 2009. Small farms were classified into six mutually exclusive and homogeneous groups (two groups of micro-farms and four groups of small farms) according to their degree of diversification and differentiation of production. For each group, the economic sustainability as well as the role of public support were assessed through a set of indicators. The results of the analysis confirm the non-economic role of micro-farms, whose justification needs rather to be found in territorial and social objectives. With regard to small farms, the results show that, even though conventional profiles are still predominant, most farms demonstrate some sort of interest in diversification and multifunctionality. The majority of farms focus on the strategy of differentiation through quality products, which is a key aspect for Italian agriculture performance and competitiveness. Finally, the indicators of economic sustainability seem to confirm the complementary role of rural development policies to the first pillar of the CAP, by highlighting the deep compensatory effect of the second pillar payments to the dynamics of income of the farm types identified.

Key words: small farms, FADN, multifunctionality, income diversification, CAP

Streszczenie. Artykuł prezentuje wyniki badań nad znaczeniem wielofunkcyjnej działalności małych gospodarstw we Włoszech, analizując zarówno zadania rolnicze, jak i pozarolnicze w oparciu o włoską bazę danych FADN (sieci danych rachunkowych gospodarstw rolnych), obejmujących okres od 2003 do 2009 roku. Małe gospodarstwa zaklasyfikowano do sześciu wzajemnie wykluczających się, jednorodnych grup (dwie grupy mikrogospodarstw i cztery grupy małych gospodarstw) w zależności od ich stopnia dywersyfikacji i zróżnicowania produkcji. Używając szeregu wskaźników, w każdej z grup dokonano oceny pod względem zrównoważonego rozwoju gospodarczego i roli wsparcia publicznego.

Corresponding author – Adres do korespondencji: dr Francesco Vanni, Istituto Nazionale di Economia Agraria, Via Nomentana 41, 00161 Rome, Italy, e-mail: vanni@inea.it

Wyniki analizy potwierdzają pozaekonomiczną rolę mikrogospodarstw, której uzasadnienia należy szukać w celach społecznych i terytorialnych. W odniesieniu do małych gospodarstw wyniki wskazują, że wprawdzie nadal dominują tu konwencjonalne struktury, lecz większość gospodarstw wykazuje zainteresowanie dywersyfikacją i wielofunkcyjnością. Gospodarstwa przeważnie skupiają się na strategii zróżnicowania poprzez wytwarzanie produktów wysokojakościowych, co jest elementem kluczowym dla wydajności i konkurencyjności włoskiego rolnictwa. Wreszcie, wskaźniki zrównoważonego rozwoju gospodarczego wydają się potwierdzać uzupełniającą rolę polityki rozwoju obszarów wiejskich dla pierwszego filaru Wspólnej Polityki Rolnej poprzez podkreślenie silnego wyrównawczego wpływu drugiego filaru płatności na dynamikę przychodów badanych typów gospodarstw.

Słowa kluczowe: małe gospodarstwa rolne, sieć danych rachunkowych gospodarstw rolnych, wielozadaniowość, dywersyfikacja dochodów, Wspólna Polityka Rolna

Introduction

During the last decade in Europe, both at the institutional and social level, an increasing acknowledgment of the important environmental and social role of agriculture has been observed. This has been translated into a new approach to public support for the primary sector, which has been reshaped around the concepts of farming sustainability and multi-functionality. As a consequence, the process of multifunctional diversification has been increasingly involving farms, that now produce not only food and fibres but also, and in a conjunct way, services and new products (often unfairly recognised as "secondary products").

From a policy perspective, a pivotal role in driving this transition towards multifunctional agriculture has been played by the so-called "second pillar of the Common Agricultural Policy (CAP)", since rural development policies contributed to extending the action field of multifunctional diversification not only to the production of externalities and pure public goods, but also to other economic activities whose social and environmental effects are of an indirect nature. Alongside this path, also policies in the first pillar of the CAP have been addressed, more effectively than in the past, to support the production of public goods and services in agriculture and to improve the environmental function of the agricultural activities, through a process of "greening" of the CAP.

The growing integration of agriculture into the rural economy has contributed to creating more opportunities of diversification within farms, even in fields distant from the mere agricultural one. More particularly, in Italy, a significant proliferation of initiatives that accompany the food production in the farms has been observed. Sometimes the new activities replace the proper agricultural activities, such as the production of services (tourism, recreational activities, educational ones, social services, and so on) as well as new non-farming products (energy, land and territory stewardship, etc.); in other cases they tend to include other segments of the food process, such as internalising some stages of the processing process, or the direct sale of farm products.

The choice of diversification often depends, to a large extent, on the approach of farms to the progressive decline and instability of agricultural incomes. Although

economic motivations are often at the roots of the diversification process, it has also been highlighted how such a choice can be driven by non-economic reasons, such as environmental concerns or social issues expressed at the local territorial level.

Given this as a background, the paper aims at exploring the role and the significance of these multifunctional activities for small farms in Italy. This objective has been pursued by analysing the evolution of a set of indicators which were used to assess and compare the performance of a group of more than 3000 farms of the Italian FADN database.

Previous literature on diversification has focused on the diffusion of these strategies among farmers and the characteristics of diversified farms in a limited period of time, as well as on the characteristic features of farms adopting diversified activities (McNally 2001, Esposti and Finocchio 2008, Jongeneel et al. 2008, Aguglia et al. 2009). Compared to this literature, the present paper focuses more specifically on the role of multifunctional activities for small farms, and it aims at comparing the different performances of conventional and diversified small farms in the long term, namely over the 2003–2009 period.

The results of this work have been used as a test to assess how solid and sustainable is the process of diversification of small farms. In other words, our research question is whether diversification is a viable strategy for small farms to survive in the long run or they are doomed to decline and eventually exit from the sector. The other relevant question is whether farms have actually adapted to the recent policy indications about diversification. The results of the analysis provide interesting feedbacks for future policy reform aimed at improving the multifunctional features of farms and, above all, at enhancing the economic sustainability of small farms that is not fully acknowledged and properly sustained by the present CAP.

Research objectives and methodology

The classification of small farms adopted in this article is based on a typology recently developed by the National Institute of Agricultural Economics – INEA (Ascione et al. 2011) based on information gathered by the Italian FADN (Farm Accountancy Data Network) from 2008. It classifies farms taking account of both farming and non-farming activities present on a farm. Generally speaking, statistics on farms, in order to ensure homogeneity and comparability of observations, refer to the sector as a whole or consider specific specialisation branches, paying scant if any attention to the "innovative" component of the agricultural and farm activities. In spite of these limitations of official statistics, the reality of agriculture and rural areas has becoming increasingly complex and multidimensional, and the farms supply is less and less limited to "conventional" agricultural products, but includes new and more complex ones, such as quality products (intended in a broad sense, that is including organic products, denominations of origin, territorial brands, and so on). Moreover, the idea of diversifying the production becomes more and more popular among European and Italian farmers, and that explains the larger combination of goods and services supplied by farms (the so-called "connected activities"), such as agro-tourism, rural

tourism, educational farms, therapeutic farms, and so on. As a consequence, statistics are catching up with these changes and focusing more neatly on reality as it is on farms and in agricultural and rural areas. The results of such an effort often lead to the taxonomy of new and different farm types, which represent, in a more accurate way, the new functions of agriculture and products associated with them.

On the basis of the farm typology developed by INEA (Ascione et al. 2011), small (commercial[1]) farms are here classified into 6 mutually exclusive and homogeneous groups according to the degree of diversification and differentiation of production, and by size. The degree of diversification and differentiation is assessed on the basis of the quota of *gross saleable production* (GSP) associated with differentiated and diversified farm products. In greater detail, the share of GSP originating from PDO products (products with protected designation of origin), organic farming products and other certified products is used to identify whether a farm is following a quality-based strategy, defined as *differentiation* strategy. The share of GSP originating from agro-tourism, on-farm recreational activities, and other services such as on-farm processing (wine, cheese, and so on) is used to assess whether a farm is adopting some *diversification* strategies. The share of the value of these types of production in the total farm GSP has been used to determine the three main types of farms: conventional, differentiated, and diversified.

The economic size is defined on the basis of the value of *total farm gross saleable production* (TFGSP). According to this indicator, and excluding from our analysis all "large farms", i.e. those for which the TFGSP value has been set above 100 000 EUR, two main classes of farms have been defined: micro-farms, with TFGSP below 15 000 EUR, and small farms, with TFGSP between 15 000 and 100 000 EUR.

The choice of using TFGSP rather than the *standard gross margin* (SGM), usually used in the main classifications of farms at the EU level, is a consequence of the objective to produce a classification of small farms that takes into account the value of quality agricultural products as well as the value of non-agricultural products (e.g. agro-tourism, etc.) produced by the farm. SGM is, by definition, a standardised value so that it does not consider the variability of sale prices according to the quality level of marketed goods and does not take into account the non-agricultural activities.

The variables and the thresholds used to segment the farms in the typology have been set up on the basis of the advice of a panel of experts (Table 1). The resulting farm typology clusters farms into the following categories:

- **Micro-farms.** This group includes very small farms which, even though classified as professional as all FADN farms, are so small that their relationships with markets are marginal if not nonexistent. Some of these farms provide various functions, so that they can be considered "multifunctional", the others are "conventional" (two sub-groups).
- **Small farms.** This group includes four sub-groups: "conventional" farms, farms slightly and strongly orientated towards quality products (respectively, "conventional quality" and "differentiated" farms), and "diversified" farms (farms running diversified activities).

[1] Farms in FADN are by definition "commercial", meaning they are market-orientated and produce for sale.

Table 1. Typology of small farms (variables and thresholds)

Variable	Micro-farms		Small farms			
	Conventional	Multifunctional	Conventional	Conventional quality	Differentiated	Diversified
TFGSP	< 15 000 EUR		15 000–100 000 EUR			
Share of quality brands in GSP	< 10%	> 10%	< 10%	10–30%	> 30%	< 30%
Share of other revenues in GSP	< 30%	> 30%	< 30%	< 30%	< 30%	> 30%
Share of agro-tourism in GSP	0	0	0	0	0	0
Share of processing in GSP	–	–	< 30%	< 30%	< 30%	> 30%

TFGSP – total farm gross saleable production, GSP – gross saleable production

Source: Authors' elaboration based on Italian FADN data

The paper, given the typologies described in Table 1, aims at addressing the following research questions:

1. What is the degree of differentiation and diversification of Italian small farms?
2. How sustainable these processes of differentiation and diversification are in economic terms?
3. To what extent the current policies are providing small farms with an effective support to increase differentiation and diversification strategies?

The degree of differentiation and diversification of Italian small farms was assessed by applying the aforementioned classification to the Italian FADN data related to 2008 and 2009.

The economic sustainability as well as the role of public support were assessed through a set of indicators which were calculated for each typology over the 2003–2009 period. This analysis was carried out on a constant group of farms, covering the period from 2003 to 2009 (the observations with incomplete or missing data were removed), obtained from the RICA (Italian FADN) sample[2]. The group comprised

[2] The Italian FADN survey started to be conducted on a statistically representative sample drawn from the census of 2003. The sample is stratified according to the following criteria: geographical region, economic size (ESU), and farming type (FT). The field of observation is the total of commercial farms, i.e. farms with an economic size greater than 4 ESU (4800 EUR). The FADN sample size is approximately 15 000 farms covering 44% of total Italian farms and 99% of utilised agricultural area (UAA).

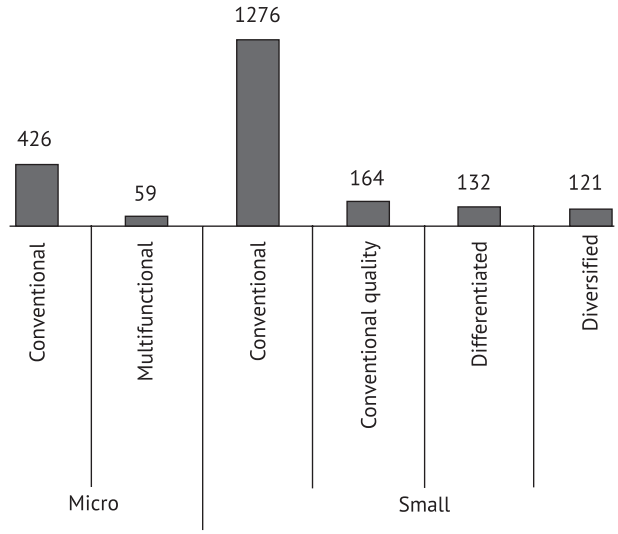
3101 units, of which 2178 were classified as micro-farms and small farms (TFGSP lower than 100 000 EUR).

With regard to the economic and public support indicators, the *farm net value added* (FNVA) and the *value added/gross saleable production* ratio (VA/GSP) were used as a proxy for farm profitability, while the role of public support was assessed through the ratio of the actual level of support coming from the CAP to the farm net income, from which one can infer the level of support ensured to each farm group.

These indicators have been calculated for the 2003–2004 and 2008–2009 periods in order to follow the economic performance of different farm groups over time. It is worth remarking that the two periods chosen correspond to two different moments of the CAP implementation: before and after the Fischler reform. This can also supply important reflections about the effects on income of the changes in policies, with specific regards to the diversification tools, and, in more general terms, on the effectiveness of public support to farm income diversification aimed at boosting competitiveness.

Results

With regard to the degree of diversification and differentiation of Italian small farms (first research question), data show that in Italy there is still a great predominance of "traditional" farms (small and micro "conventional" farms) rather than more "innovative" units such as the diversified and the differentiated farms (see Fig. 1).



Source: Authors' elaboration based on FADN data

Fig. 1. Number of farms by type

Indeed, conventional farms represented 78% of the total number of farms. Within the conventional profiles, the largest group is that of small conventional, which includes 1276 units. At the same time, figures highlight that the conventional profiles also show some sort of interest towards diversification and multifunctionality, through the realisation of certified products and denominations and also through secondary functions connected to agricultural production. However, this share of inputs and resources devoted to differentiation and diversification activities is only marginal compared to the total production. This tendency seems to confirm the idea that a certain level of multifunctionality and diversification is actually present on most farms (Henke 2004, Wilson 2007, 2008, Henke and Salvioni 2008).

The number of micro-farms in the group is relatively high: 485 units, of which only 59 can be considered as following a multifunctional approach to the primary activity. This is a hint about the role of entrepreneurial skills necessary to undertake a path of farm diversification, which are easier to find in relatively larger farms than in micro ones.

If we draw our attention to the "innovation" strategies (diversification and differentiation), the majority of small farms are focused on the strategy of differentiation through quality products, since 9.7% of small farms can be classified as conventional quality and 7.8% as differentiated farms.

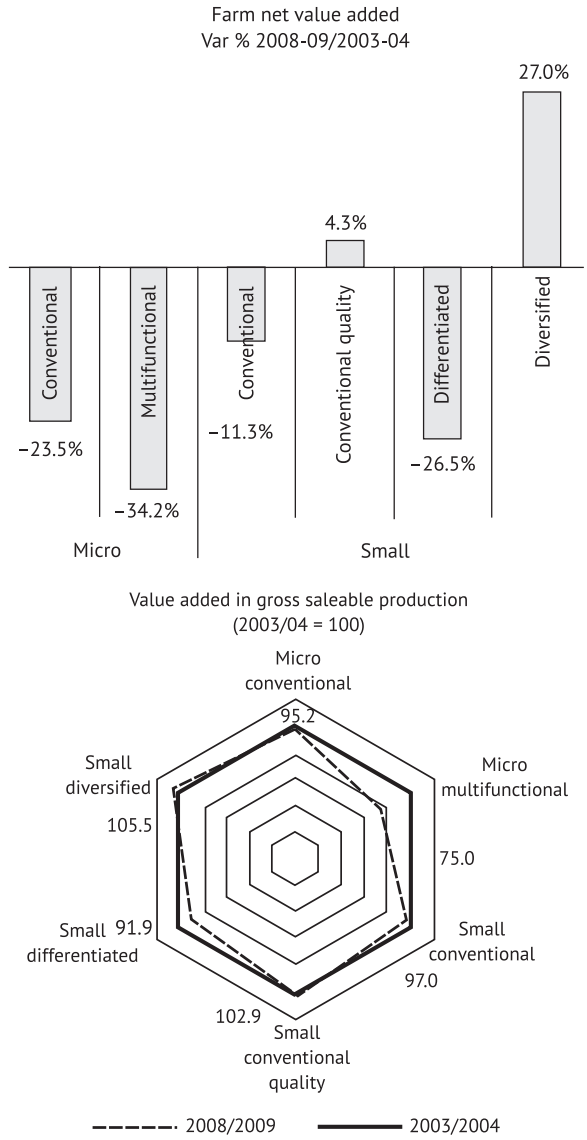
Referring to Van Der Ploeg categories of multifunctional farms (Van der Ploeg and Roep 2003), the farms we studied seem more orientated to deepening functions rather than broadening ones. More specifically, the agricultural deepening task is pursued through the realisation of quality products (organic farming, PDOs, traditional products, other denominations), which are all aimed at increasing the value added within the primary component of the production chain.

As discussed in the previous section, the economic performance of the different types of farms was also calculated (second research question), in order to show the variations, for the two periods considered, of the main variables characterising the structural and economic features of the farms.

Figure 2 shows the results related to the *farm net value added* (FNVA), which is an estimate of the value added of farms net of mortgages and taxes, but including public support, and the share of *value added in the gross saleable production* (VA/GSP), which can be considered the gross margin produced by the farm, net of any type of costs, both fixed and variable.

Data show that diversified small farms achieved a better economic performance over the period considered compared to the other profiles, both in terms of FNVA (+27.0%) and in terms of VA/GSP (+5.5%). With regard to the differentiation strategies, the results are quite encouraging for small conventional quality farms, which have experienced a slight increase in both FNVA (+4.3%) and VA/GSP (+2.9%), while for the differentiated farms it is possible to observe a decline in FNVA (–26.5%) and in VA/GSP (–8.1%).

Finally, it is worth underlining the performance of micro-farms, which represent one fifth of the group composition. The negative economic performance of these farms is an indirect confirmation of their non-economic role, whose justification needs to be rather found in territorial and social objectives, and suggests that they are at risk of disappearing if not supported by adequate and targeted policies.

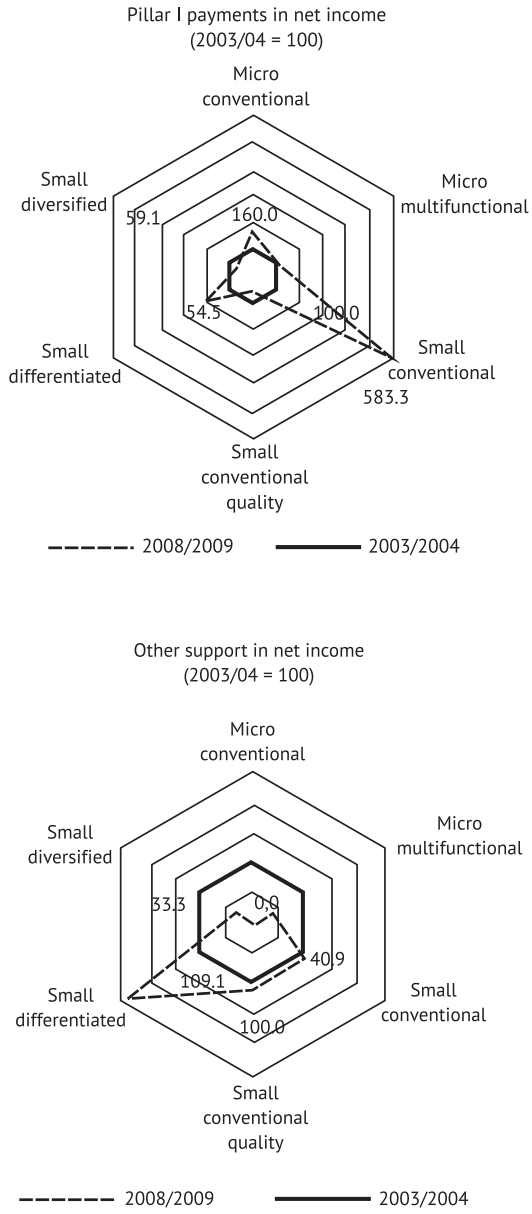


Source: Authors' elaboration based on FADN data

Fig. 2. Economic performance of different types of small farms (2003/2004 – 2008/2009)

With regard to the role of public support for small farms (third research question), indicators show how the net income, realised by different farm profiles, is supported on average by public support from the first and second pillar of the CAP and other regional payments (see Fig. 3). In particular, the support from the first pillar (decoupled single payment and specific coupled support) is included in the value of GSP. By

contrast, the other support including payments from the second pillar through Rural Development Plans (RDPs) and regional payments, such as state aids, are not included in the value of GSP.



Source: Authors' elaboration based on FADN data

Fig. 3. Public support for different types of small farms (2003/2004 – 2008/2009)

Data show how the economic performances of different profiles in the period observed are all generally boosted by public support, coming from both the first pillar and other sources. However, it is worth noting that there is a sort of complementarity effect between different sources of support, so that if one category is under-dimensioned, the other will at least partially compensate.

Given the strategic choices of farms, conventional farms usually integrate their revenues with support coming from the first pillar of the CAP (during the period observed, the support from the first pillar has increased for both the micro and small conventional farms). The higher component of support from the first pillar could be due to their prevailing specialisation in highly supported sectors such as intensive livestock production. Income for small diversified (–41%) and small differentiated (–46%) farms is relatively less supported by direct payments, while other forms of support are much more important in integrating their revenues, especially in the case of small differentiated farms (+9%). This is particularly due to the rural development policies and specifically to the quality measures in the second pillar of the CAP.

Figures also show that even micro-farms experienced a large increase in the share of first pillar payments in net income (+60%), while interestingly enough the variation of support coming from the second pillar is null or even negative in the case of multifunctional micro-farms (–59%).

These results confirm that there is a sort of complementarity between the pillars of the CAP in providing income support to Italian farms, no matter what their strategic path is. Indeed, such complementarity is the consequence of the overall picture of the support policies that, to a large extent, have been drawn to be complementary.

Conclusions

The main issues that have emerged from the analysis presented here, in terms of the characteristics and role of small farms, may be summarised as follows:

- The results of the analysis confirm the non-economic role of micro-farms, whose justification needs rather to be found in territorial and social objectives. Their economic performance has worsened with time, in spite of a significant improvement in the public support coming from both pillars of the CAP. As a consequence, the opening of these farms to diversification issues has probably more to do with the possibility of having access to public financial resources rather than pursuing real diversification strategies. Their diversification path is preferably directed towards acquiring new functions in the agricultural chain (deepening functions), such as direct sale or farm processing, rather than towards diversifying into non-agricultural on-farm activities (broadening activities). This is probably due to the lack of start-up capital and of entrepreneurial skills.
- Conventional profiles show, to some extent, some sort of interest towards diversification and multifunctionality, through the realisation of certified products and denominations and also through secondary functions connected to agricultural production. This tendency seems to confirm the idea that most farms, irrespective of their size and their territorial relationship, actually exhibit a certain level of

multifunctionality and diversification. The hypothesis of a "spectrum" of multifunctionality in post-productivist agriculture is confirmed by this analysis.

- As regards the "innovation" strategies (both diversification and differentiation), the majority of farms in the group focused on the strategy of differentiation through quality products, which is crucial to Italian agriculture performance and competitiveness. More generally, the farms of the group seem more orientated to deepening functions rather than broadening ones.

With regard to the role of public support for diversification and differentiation strategies, the indicators of economic sustainability seem to confirm the complementary role of rural development policies to the first pillar of the CAP, by highlighting the deep compensatory effect of the second pillar payments to the dynamics of income of the farm types identified.

From this perspective, many studies have shown that although traditional structural policies have been largely ineffective in overcoming the structural problems of small farms and in adjusting them to modern standards and techniques, first pillar policies often result in little lump-sum payments that complement farm household income up to the survival level, but that do not allow farmers to become independent from the welfare redistribution sphere, to reverse marginalisation and to solve the chronic low income problem. It is like they freeze the condition of farms, preventing them from exiting the sector but also from developing entrepreneurial skills so as to react and reverse the marginalisation process.

The economic sustainability of small farms could be better addressed through second pillar policy measures, especially those orientated towards the diversification and differentiation of farming activities, because they require a pro-active attitude to farmers, who need to prove their ability to change and negotiate with institutions on their entitlement to have access to public support.

Nevertheless, the results so far achieved through rural development policies could be largely improved by increasing the financial resources of the related measures, by decreasing the complexity in terms of accessibility to funding and, above all, by focusing more on improving farmers' skills, education and knowledge (i.e. to deal with production and markets).

From this perspective, it must be highlighted that, on the one hand, the EU Commission CAP proposal for 2014–2020 strongly emphasises the importance of knowledge and innovation for farmers, also by focusing on the development of local networks of different stakeholders in rural areas, which could have interesting implications for the competitiveness of small farms. On the other hand, the current proposal seems quite ineffective in identifying specific forms of support for small farms, tailored to the different territories and to the structural features of farms. On the contrary, the simplified scheme of support for small farms goes once again in the direction of offering low but "safe" income integration, not enough to reverse the slow decline but enough to keep on a path of marginality and subsistence.

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