The implications of further CAP Reform on the regional impact of livestock headage payments in Scotland

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Why analyse the spatial impacts of the CAP?

The Common Agricultural Policy (CAP) is the single largest policy of the EU in expenditure terms, accounting for 44 per cent of the budget in 1998[2]. Its basic remit is for increased agricultural productivity, a fair standard of living for those engaged in agriculture, stable markets, assured supplies and reasonable prices (Article 39 of the Treaty of Rome). The redistribution of wealth from prosperous to poorer countries and regions is not overtly a CAP objective. The nearest the CAP comes to such a focus is in the LFA Directive, where one of the objectives is to "maintain a viable agricultural community and thus help develop the social fabric of rural areas by ensuring a fair standard of living for farmers and by offsetting the effects of natural handicaps in less-favoured areas;…" (EU Regulation 950/97). However, whether intentional or not, all sectoral policies have significant (sometimes substantial) spatial impacts, which either reduce or exacerbate regional disparities in prosperity and income. This paper attempts to assess the livestock subsidy regime of the CAP in Scotland, and the proposed future reforms, in terms of their unintentional regional impact. The context for this analysis is the EU's cohesion objective (a basic pillar of the Treaty of Union) together with the more recent focus on spatial planning through the European Spatial Development Perspective (ESDP).

The First Report on Economic and Social Cohesion (EU Commission, 1996) quotes from Article 130a of the Treaty of European Union where cohesion "is set in terms of 'harmonious development' with a specific geographical dimension: 'reducing disparities between levels of development of the various regions and the backwardness of the least favoured regions, including rural areas'". It goes on to develop these ideas in terms of quality of life, income disparities, competitiveness and equality of employment opportunity.

Chapter 4 of the Cohesion Report discusses the contribution to cohesion made by different EU policies. The effect of the CAP, although not explicitly formulated with cohesion in mind (as for instance Structural Policy is), is held to be benign, since it results in transfers from taxpayers and consumers (through subsidies and increased retail prices) in net contributor countries and relatively wealthy regions where agriculture is not an important economic sector, into net recipient countries, and poorer agriculturally dependent regions. The 1992 Reforms are held, on the whole, to have enhanced these redistributional effects[3].

The ESDP is essentially an attempt by the Committee of Spatial Development (DG XVI), to create a strategic planning framework to ensure that both EU and national policies (including the CAP) become more compatible with the triple objectives of cohesion, balanced regional competitiveness, and sustainable development (EU Commission, 1997; 1998, Williams, 1996). Whilst the ESDP document, drafted for the Noordwijk meeting of ministers in June 1997 and revised for the Glasgow meeting in June 1998, is not legally binding, it is intended to "be the expression of a shared vision of the European Territory as a whole, a common reference framework for action, and to guide the relevant authorities in policy formulation and implementation" (EU Commission, 1998).

The ESDP reiterates the conclusions of the Cohesion report regarding the redistributional impacts of the CAP and the 1992 reforms, stressing the increased support for "weaker regions and countries with a greater proportion of the workforce in agriculture" (Ibid). It also, however, suggests that the CAP has had the effect of concentrating production on "land that is most appropriate for modern methods of farming" (Ibid), with associated environmental and landscape impacts. Furthermore, set-aside compensatory payments are portrayed as working against cohesion. "In terms of support for farm incomes, this approach has generally benefited those parts of the EU which are already more intensively farmed since payments were based on historic yields" (Ibid). The document is luke-warm in its enthusiasm for the agri-environmental and livestock extensification elements of the reforms. The section concludes:

"In summary, the CAP is not neutral in its effects on the territory of the EU. Some have been positive, others negative but these effects need to be more systematically identified and evaluated than has been done so far."

It is the aim of this paper to make a contribution to the development of simple methodologies to advance this evaluative process.

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[1] Rural Policy Group, Scottish Agricultural College, Aberdeen.

[2] EU (1998) Preliminary Draft General Budget of the European Community for the Financial Year 1999.

[3] However it is noted that the experience of different member states varies widely. With respect to the UK it is suggested that the Reforms have "slightly accentuated" disparities between prosperous and more marginal rural regions.

Regional targeting of support through livestock headage payments in Scotland 1990-97

(a) The situation before the 1992 reform

The analysis which follows is based upon research carried out for Highlands and Islands Enterprise, which used an established regional output estimation procedure to assess the impact of CAP Reform on the Highlands and Islands of Scotland. This methodology estimates output by district for 24 separate crop and livestock enterprises, on the basis of Agricultural Census data and per hectare or per head coefficients derived from a variety of sources[4]. Scottish expenditure on 10 direct subsidies are apportioned to districts in a similar way. UK market support expenditure for the main products is apportioned according to share of crop output and livestock numbers in each district. In accordance with the theme of this conference, this paper will focus on the livestock sector only. Throughout the following analysis, tables of results will group the fifty-six Scottish districts according to EU Structural Fund designation (for details see Appendix 1). This classification reflects the basic pattern of regional disparities in Scotland, and is a useful structure within which to assess the redistributive impact of livestock subsidies.

Figure 1(a) shows that before the 1992 reforms hill and upland livestock farming, especially in the north and west of Scotland, was already much more heavily subsidised than that of the lowland areas. In some areas, especially Skye and Lochalsh, the Western Isles and Shetland, more than 35 per cent of livestock output was attributable to subsidies. By contrast, in many of the predominantly low-ground districts of the south and east, the contribution of subsidies to livestock output was less than 25 per cent.

The explanation of this contrast obviously lies in the fact that the majority of headage payments (Suckler Cow Premium (SCP), Sheep Annual Premium (SAP), and Hill Livestock Compensatory Allowances (HLCA)) were (and still are) payable on breeding stock, which are concentrated in the uplands. Furthermore HLCAs are paid only to ewes and beef cows on farms in the Less Favoured Area (LFA), and at higher rates within the Highlands and Islands, whilst the SAP scheme offers an enhanced premium to LFA ewes. Market support payments (accounting for about 40 per cent of all subsidy expenditure at this time) are viewed as benefiting both lowland and upland farmers[5], and hence in this analysis were apportioned according to total number of cattle and ewes.

The implications of the pattern shown in Figure 1(a) for regional targeting and cohesion can be seen more clearly if the districts are grouped according to Structural Fund Objective. This is a classification intended to represent a broad consensus with regard to lagging or disadvantaged areas which might reasonably be the focus of any regional targeting of the CAP in furtherance of the Cohesion Objective[6]. Table 1 shows that in the 1990-92 period livestock subsidies accounted for on average 31 per cent of livestock output in the Highlands and Islands Objective 1 area. In the Objective 5b areas the proportion was a little under 20 per cent, and in the non-objective and mixed

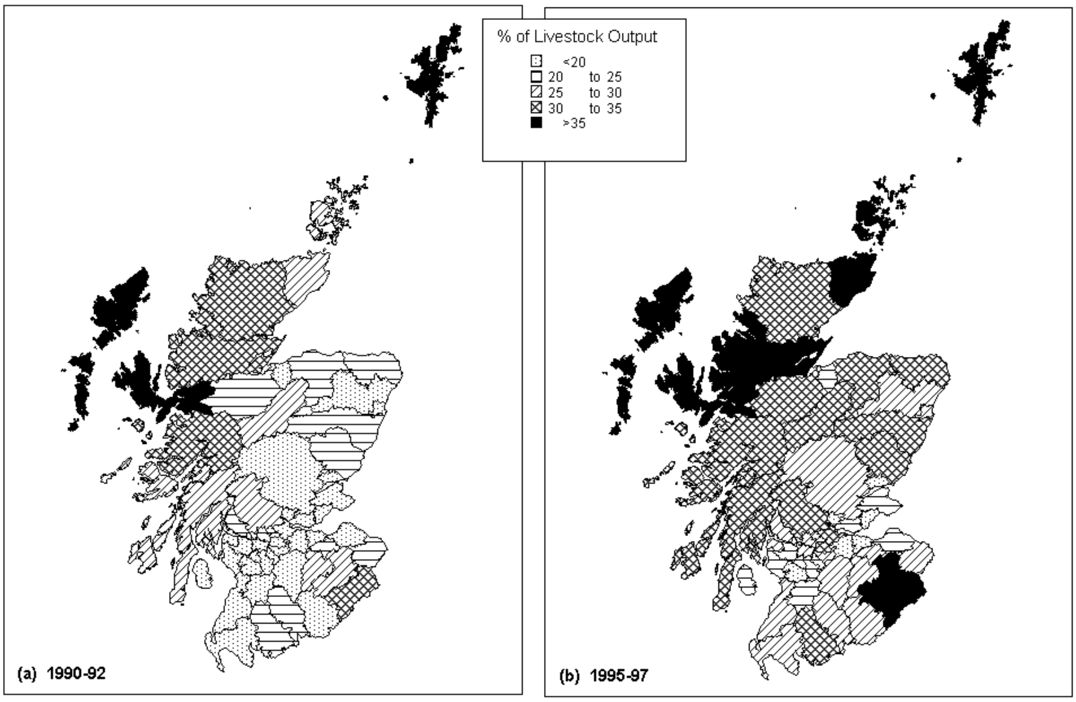

Figure 1. Percentage Livestock Output Derived from Subsidies.

[4] Full details are given in Copus (1995).

[5] Through enhanced store stock prices.

[6] The poor fit between districts and Objective 5b areas in Scotland means that the figures in Table 1 are approximate. Details of the classification of Districts are given in Appendix 1.

Table 1. Livestock Subsidies in Scotland 1990-92 and 1995-97 by Structural Fund Objective Area (1 Euro = £0.631).

Tota	Total Livestock Subsidies 1990-92 mEuro 1997 prices	1995-97	% of Livestock Output 1990-92 %	1995-97 %	Change %
Obj. 1 Highlands and Islands	120	157	30.6	37.0	30.6
Obj. 5b	171	240	19.9	27.8	41.3
Non Obj/Mixed Areas	162	238	16.5	24.9	47.0
Scotland	**453**	**635**	**20.3**	**28.3**	**40.5**

Table 2. Livestock Subsidies in Scotland 1990-92 and 1995-97: Share of Scottish Total by Structural Fund Objective Area.

	Share of Scottish Total 1990-92 %	1995-97 %	Change in Share %
Obj. 1 Highlands and Islands	26.5	24.6	-7.0
Obj. 5b	37.8	38.0	0.6
Non Obj/Mixed Areas	35.7	37.4	4.6
Scotland	**100.0**	**100.0**	**0.0**

districts it fell to 16 per cent. This suggests that in the period immediately prior to CAP Reform the livestock subsidy regime was quite successful in directing support towards regions in which the economy in general was lagging behind. In other words it could be considered to be making a positive contribution towards the Cohesion objective.

(b) The effect of the 1992 reform

The 1992 CAP Reform enhanced the role of headage payments relative to market support, the latter accounting for approximately 25 per cent in the 1995-97 period[7]. At the same time, however, the targeting of direct support became a little less focussed as more expenditure was made through the untargeted BSP, SCP and SAP schemes, and relatively less through HLCAs[8].

As Figure 1(b) shows, almost every district in Scotland saw an increase in the percentage of livestock output derived from subsidies in the 1995-97 period. Table 1 shows that the Objective areas continued to receive more subsidy per unit of output than the non-Objective and mixed districts. However, the rate of increase was lower in the Objective areas, the Highlands and Islands receiving an increase of 30% compared with 41% in the Objective 5b areas and 47% in the undesignated areas. This suggests a slight weakening in the targeting of support. This conclusion is supported by Table 2 which shows that the Highlands and Islands' share of the total Scottish livestock subsidy fell by 7% between 1990-92 and 1995-97. The Objective 5b share was almost static between these two periods, but the non-designated areas increased their share by almost 5%.

It therefore seems reasonable to argue that in terms of the livestock sector in Scotland the 1992 CAP Reforms had a slightly negative impact upon the compatibility of the policy with the Cohesion Objective.

The current reform proposals

It is clearly beyond the scope of this paper to give a full account of the proposed further reform of the CAP. However, a brief outline of the changes to the livestock regime (as proposed in the draft directive of 18 March 1998[9]) will provide a context for the following analysis.

In the dairy sector, a progressive 15 per cent reduction in institutional prices, and a 2 per cent increase in global quota, is to be accompanied by the introduction of a Dairy Cow Premium (DCP). This is intended partly as compensation for milk price cuts and partly to offset the effects of the proposed 30 per cent cut in beef institutional prices. Partial compensation for the latter is also proposed in the form of increases to BSP and SCP payments. The sheep sector escapes the reform proposals unscathed.

A very important additional complication in the proposed reform is the suggestion that one-third of direct livestock

7 The proportion would in fact have been rather lower but for some fairly large BSE-related expenditure in 1996 and 1997. The percentage was down to 10 per cent in 1995.

8 HLCAs are 25 per cent nationally funded, and are therefore a more expensive form of support as far as the UK government is concerned.

9 The research on which this paper is based was completed in May 1998.

subsidy expenditure will be set aside from the mainstream schemes into “national envelopes”, allowing member states to allocate it either according to cattle numbers or according to the area of permanent pasture (see Appendix 2 for details). This has been seen in some quarters as the “thin end of a re-nationalisation wedge”. It must be said, however, that the proposals do not allow any national expenditure, and the way in which the “national envelopes” can be spent is circumscribed by specific limits per head and per hectare. Nevertheless, they do represent a very important opportunity to strengthen the spatial targeting of livestock subsidy.

A further proposal affecting the livestock sector is that HLCA payments could be transferred from a headage to an area-based allocation. Again, as we hope to show through the following analysis, this is an option which opens up considerable possibilities in terms of spatial targeting.

(a) Three scenarios for the impact of reform

Using the district output estimates for 1997 as a starting point, the impact of the proposed reforms on livestock output and the distribution of subsidy may be forecast with reference to three scenarios[10]:

Scenario 1 assumes that 75 per cent of the institutional price cuts are reflected in market prices in Scotland. It also assumes a 10 per cent devaluation of the green pound in relation to the ECU (compared with 1997 average rates). Furthermore it is assumed that all the livestock subsidy national envelope would be paid through an increase in headage payments (including the new DCP). Market support is assumed (perhaps unrealistically) to be zero.

Scenario 2 has the same currency and price assumptions as Scenario 1, but differs in the allocation of the national envelope to area-based payments.

Scenario 3 is identical to Scenario 2 but in addition assumes that Scottish HLCA payments would be allocated (like the National Envelope expenditure) according to permanent grass area.

(b) Likely regional impacts

Under Scenario 1 total direct subsidy expenditure in Scotland is estimated to rise from the 1995-97 average of £296m to 545m Euro, and to account for almost 26 per cent of livestock output (Table 3). The increase would not, however, be uniform across the country, with the largest increases (30 per cent) being in the districts outside the Structural Fund Objective areas. Subsidies to the Objective 5b areas would increase by only 14 per cent, whilst those to the Highlands and Islands would be almost static. In terms of share of the Scottish total the Highlands and Islands would actually see a fall from 28 per cent to 24 per cent (Table 4). Clearly this implementation of the proposed reforms would not contribute very much to reducing regional disparities.

Scenario 2, however, in which the National Envelope expenditure is apportioned according to permanent grass area, is rather more “cohesion-friendly” in terms of its regional impact. Under the assumption of a single per hectare rate for the UK, Scotland would gain at the expense of England and Wales, due to the prevalence of more extensive grass-based production. The largest increase in subsidy (81 per cent) would be in the Highlands and Islands, and the smallest (40 per cent) in the Objective 5b districts. In the un-designated and mixed Districts the increase would be 50 per cent. In terms of their share of the Scottish total, the Highlands and Islands would gain substantially relative to the 1995-97 distribution, whilst both the Objective 5b and undesignated/mixed districts would receive a smaller share.

Under Scenario 3, (which also assumes that the 1997 total Scottish HLCA expenditure would be apportioned according to permanent grass area) the Highlands and Islands would receive an even larger share of the total Scottish subsidy (36 per cent), representing a more than 100 per cent increase on the 1995-97 figure. Again the non-designated/mixed Districts would receive the second largest increase, of over 40 per cent, but see a small decline in their share of the Scottish total relative to 1995-97. The Objective 5b districts would receive the smallest increase, of 33 per cent, and see a decline in their share of over 9 per cent.

Conclusions

The ESDP calls for the regional impacts of the CAP to be systematically identified and evaluated. Although there is considerable scope for refinement, the analysis of output and subsidy distribution presented above illustrates a potential methodology for fulfilling this requirement.

Table 3. Livestock Subsidies and Output, Scenarios 1-3 by Structural Fund Area (1 Euro = £0.631).

	Total Direct Livestock Subsidies				% of Livestock Output			Change
	1995-97	S1	S2	S3	S1	S2	S3	1995-97-S3
	mEuro 1997 prices				%	%	%	%
Obj. 1 Highlands and Islands	129.8	131.2	235.2	261.6	34.9	49.0	51.7	101.4
Obj. 5b	179.9	205.4	253.1	239.5	24.9	29.0	27.8	33.1
Non Obj/Mixed Areas	159.7	207.9	238.2	225.4	22.6	25.1	24.1	41.1
Scotland	**469.4**	**544.5**	**726.5**	**726.5**	**25.7**	**31.5**	**31.5**	**54.7**

[10] Full details are presented in Copus and Bowley (1998).

Table 4. Share of the Scottish Total Livestock Subsidies, Scenarios 1-3 by Structural Fund Objective Area.

	Share of Scottish Total 1995-97 %	S1 %	S2 %	S3 %	Change in Share 1995-97-S3 %
Obj. 1 Highlands and Islands	27.7	24.1	32.4	36.0	17.1
Obj. 5b	38.3	37.7	34.8	33.0	-9.1
Non Obj/Mixed Areas	34.0	38.2	32.8	31.0	-3.6
Scotland	**100.0**	**100.0**	**100.0**	**100.0**	**0.0**

The results show that the pre-1992 CAP livestock subsidy regime in Scotland had an effective, regional redistributive effect, focusing support on economically lagging areas such as the Highlands and Islands Objective 1 area and the Objective 5b areas of Stirling, Tayside, the Borders and Dumfries and Galloway. This was partly intentional, through LFA policy, but also, partly an unintentional result of sectoral policy decisions which allocated the majority of direct subsidies to breeding stock.

The 1992 Reforms, together with national decisions regarding HLCA rates, resulted in a significant weakening of the cohesion benefits of the livestock sector CAP in Scotland. However, the current proposals present a valuable opportunity to ensure that the CAP continues to play a role in reducing regional disparities (at least with respect to the Highlands and Islands), providing the National Envelope is allocated on a per hectare basis. A move to area-based HLCAs would further enhance targeting on the Highlands and Islands Objective 1 area.

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[11] Where a district is roughly equally divided by the Objective 5b boundary it has been allocated to the “Non-Assisted and Mixed” category, since the majority of its population and economic activity would be located outside the boundary.

Appendix 1

Structural Fund Areas in Scotland

Figure A1(a) shows the Scottish designations under Objectives 1 and 5b. Since several of these (Objective 1 Highlands and Islands and Objective 5b in Grampian and RuralStirling/Upland Tayside), do not conform to any commonly used administrative boundary, an approximation to the two designations (Fig A1(b)) has been created as a basis for regional comparisons.[11]

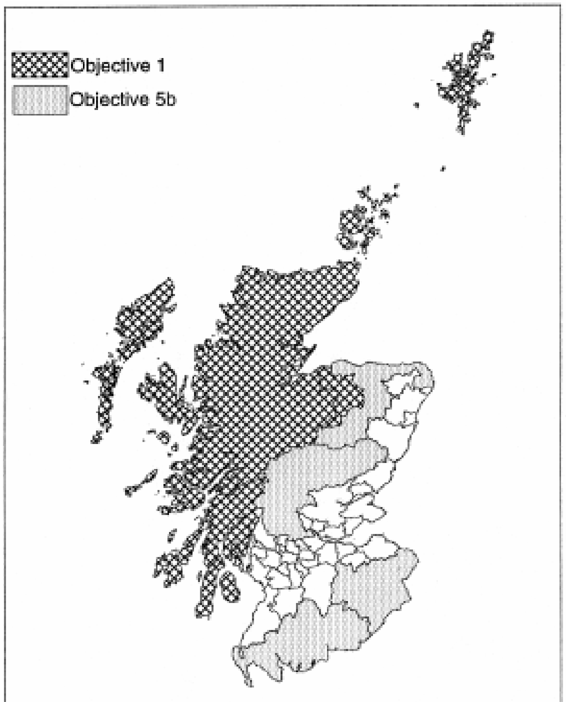

Figure A1(a): Objective 1 and 5b Areas in Scotland

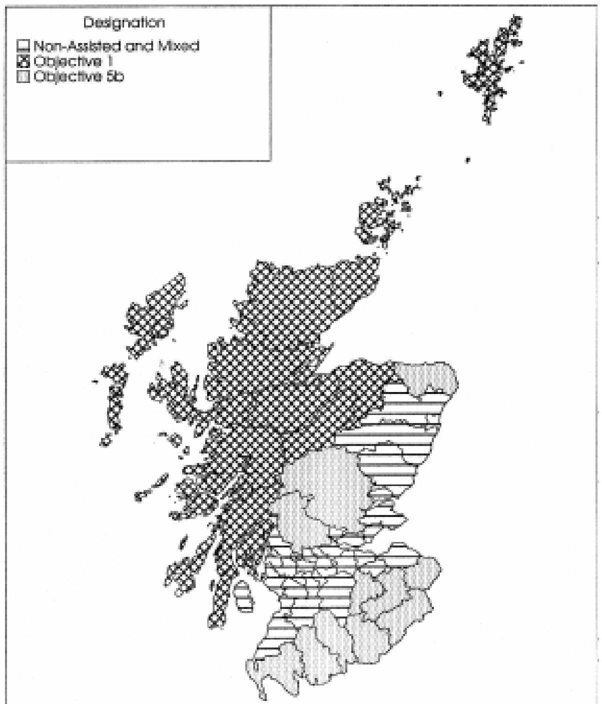

Figure A1(b): Districts by Structural Fund Designation

Appendix 2

The National Envelope Proposal

According to this proposal the total value of each of the main subsidies (Beef Special Premium [BSP], Suckler Cow Premium [SCP], and DCP) will be reduced by approximately one-third, in order to provide funds for the "national envelopes". These funds can be paid at the discretion of the member states either according to permanent grass area, or (within specific limits) as top up payments on bulls, steers, suckler cows, beef heifers or dairy cows. These payments will also have to be within strict limits per hectare. The basic premium rates and limits are shown in Table A1.

Table A1. Proposed Livestock Premium Rates (Euro per head).

		1997/98	2000	2001	2002	2003
Bulls	*Basic Premium* *Maximum Amount*	135	165 210	195 280	220 355	220 355
Steers	*Basic Premium* *Maximum Amount*	108.7	130 320	150 420	170 530	170 530
Suckler Cows	*Basic Premium* *Maximum Amount*	144.9	155 175	170 205	180 235	180 235
Heifers	*Maximum Amount*		100	150	225	225
Dairy Cows	*Basic Premium (dairy)* *(beef)* *Maximum Amount*		25 12 90	50 23 180	75 35 270	100 35 330
Max Area Payment			210	280	350	350

Source: Agra Focus April 1998.