

CAP IN HAND

ED HAMER asks if the Single Farm Payment has facilitated the consolidation of farmland in our own green and pleasant land.

Even if you're not an avid reader of *Farmers Weekly* you should be aware that something is happening with Europe's Common Agricultural Policy (CAP) this year. All the usual signs are there as the *Today Programme* wheels out farming commentators with carefully scripted opposing views, while *The Guardian* assures its readers that they really are in touch with the countryside, with a liberal guide to how negotiations will affect the price of their skinny-latté.

Yep – it's that time when the CAP undergoes a regular overhaul of its objectives, policies and payments in order to satisfy both the changing market and the modernising farmer. The 2013 reforms mark the end of a 10-year process which has brought the CAP in line with market liberalisation rules laid down by the World Trade Organisation in Doha in 2001. But despite the starring role played by the Policy in the collapse of recent EU budget negotiations, few people are still aware of the impact it has on what we farm, how we farm and ultimately who owns our farmland today.

The policy was introduced in 1962 in order to square the protectionist agriculture policies of the six European founding members - with the free trade principles of the Common Market established in 1957. Prior to this, these countries had successfully managed their food supplies through a combination of subsidy payments made directly to farmers (direct payments), as well as taxes used to maintain production and regulate both food imports (levies) and exports (tariffs).

Before the introduction of the CAP small countries like Luxembourg - who weren't self sufficient in food – kept levies low to ensure cheap food imports, while countries like France used high levies to protect their domestic producers. National policies also offered a degree of protection for traditional farming cultures. Italy for example imposed higher levies on items it grew well - like olives and grapes – while lowering them on dairy and meat products which it imported from pastoral countries like the Netherlands and Germany¹.

Inevitably the new Common Market couldn't accept goods that were heavily subsidised in one region competing with goods produced a few hundred miles away with no subsidy at all. The original CAP was therefore introduced to "level the playing field" and ensure that a dairy farmer in Belgium could sell milk across the border in the Netherlands without being hit with import levies or undercut by subsidised Dutch producers.

As a condition of access to the Common Market, member states agreed to surrender their direct payments and income from import levies to a central pot which was overseen by the European Commission (EC). The Commission was then given the power to redistribute the CAP budget in the way it saw fit - in order to balance the farm livelihoods and productivity of each of its member states with the food security of the European Community as a whole.



For the best part of fifty years the Policy has struggled to meet these challenging and often contradictory goals. Along the way there have been some monumental cock-ups - from the 1968 Mansholt plan which actively encouraged five million farmers to leave the land, to the MacSharry reforms of the 1990's which pitched European farmers against global producers in an effort to encourage competition and keep food prices low².

The environment has been one of the most significant casualties of the experiment, as farmers, naturally, tailored production to maximise their profit from the Policy's direct payments. And while the grain mountains and milk lakes of the 1980s will remain the enduring images of this calamity, the decimation of our topsoils, wildlife and traditional farming cultures are arguably the greatest price we've so far paid for the benefit of hindsight.

In an effort to address the embarrassment of farmers being paid to produce, regardless of demand, recent reforms of the CAP have focussed on "de-coupling" support from direct payments and instead making payments based on the "environmental

and social services good provided by our farmers as stewards of the countryside”³. Central to this decoupling has been the introduction of the Single Farm Payment scheme (SFP) which reallocated payments in 2005 from a production, to an area basis. In other words farmers are now paid according to the number of acres they farm.

Today the SFP is arguably the backbone of commercial farming in the UK and is classed by the EC as “Pillar I” support. In 2011 UK farmers claimed £3.4 billion in direct support from a total EU budget of £36 billion⁴. Colloquially the SFP may be ridiculed for its complicated and onerous paperwork, but as every sensible farmer knows, getting to grips with how it works is well worth the trouble.

To claim a Single Farm Payment you must firstly hold Single Payment Scheme (SPS) entitlements. SPS entitlements were allocated on 16th May 2005, one entitlement for each hectare of eligible farmland. Entitlements are classed by land type with each of these translating to an annual per-hectare “basic area payment”. In 2011 Lowland payments were set at £258.50 per hectare while Upland grazing received £207.72 per hectare⁵.

To claim the basic payment you do not have to be farming your land; you simply have to keep each hectare in good agricultural and environmental condition (GAEC). GAEC requirements are legally binding and relate mostly to soil conservation and maintaining biodiversity and watercourses. In reality achieving GAEC can be as simple as running a topper over pasture once every few years, controlling invasive plants and keeping hedgerows trimmed and tidy.

If you choose to turn your hand to a bit of farming, however, further requirements must be met relating to stocking densities, limiting runoff of fertilisers, pesticides and slurry, maintaining field boundaries and a percentage of permanent pasture for wildlife. These requirements are known as “cross-compliance measures” and are inspected on roughly one percent of farms claiming the SFP each year.

On top of basic payments, there are a series of additional agri-environment payments (Pillar II support) allocated each year by Natural England under the Environmentally Sensitive Area, Entry Level and Higher Level stewardship schemes. Eligibility for these payments depends on a points system based on existing biodiversity on the farm and farmers are rewarded financially for specific actions which maintain or enhance the environment.

Of course, if you own land on which you hold entitlements you are also able to sell them off or lease them to the highest bidder. Remarkably, although SPS entitlements were awarded to individuals free of charge back in 2005, they were not tied to specific plots of land. As a result they have since become a tradeable commodity in their own right, willingly facilitated



To many people the SFP is simply paying farmers for what they should be doing anyway - farming responsibly

by land agents up and down the country. Indeed you do not have to manage any land, or even take an interest in farming, in order to take a gamble on the entitlement market.

It's a fair observation that the Single Farm Payment has come to be regarded as a given right by the majority of UK farmers and makes a significant contribution to the farm's annual turnover. In 2011, 105,000 individual holdings claimed an average of £33,000 in basic payments, with 83 percent of these farms claiming additional agri-environment payments averaging £5,700 each⁶. It's worth remembering that these payments are awarded in addition to what can be earned from the land through good old honest farming.

The Fat of the Land

Since its introduction in 2005 the majority of controversy surrounding the SFP has focussed on the inequality of an area payments system which automatically awards the fattest subsidy cheques to our largest landowners. *The Land* has reported regularly on the work of *Farmsubsidy.org* which campaigns, using Freedom of Information requests, to publicise details of payments to individuals and companies made under the CAP. In March 2012 the mainstream farming press and the NFU condemned as “selective” a BBC Panorama documentary which detailed how non-farming investors have “made millions” from buying and selling SPS entitlements since 2005⁷.

Aside from these headline-grabbing figures however, there is another side to the story. An emerging trend suggests that the SFP is not only subsidising production, but also providing cash for reinvestment to medium and large-scale farmers. This is undeniably a contentious issue. While for many farmers the SFP offers a genuine safety-net in a notoriously volatile industry, there is evidence that a significant number of farmers are reinvesting their subsidy cheque into new farmland as it becomes available, prompting a concentration of both farm subsidies and farmland into fewer and fewer hands.

The Jolly Farmer

Like most people living and working in the countryside I've been aware of the SFP as a talking point but never really paid that much attention to how it actually worked or its significance to my local farmers. Until, that is, a chance conversation in the local pub got me thinking. A local farmer was cheerfully explaining how business was going well – he was getting a good price for store lambs, the beef market was firming-up and, because of the strength of the Euro against Sterling, he'd just received a £900 bonus on what he was expecting from his single farm payment. He explained that he was keen to reinvest his cheque in more farmland as it was the most secure place for him to keep his money.

I was keen to find out if this jolly farmer's story was more widespread than we'd like to believe, and in particular what impact it could have on new entrants in the sector who often struggle to get a hold on the farming ladder. The majority of new entrants face little choice but to start out renting or buying a small plot of land, a job no doubt made significantly harder when the competition is effectively subsidised by the State.

Farmer-Buyers

Land price inflation is a universal truth, immortalised in the words of Mark Twain when he said "Buy land – they ain't making it anymore". On an island of 243,000 square kilometres we are perhaps more aware of it than most, with average UK land prices climbing consistently throughout the past half-century. But as any estate agent will tell you – there is more to a valuation than simply bricks and mortar.

Ian Bailey, head of rural research at Savills Estate Agents, has been researching and digesting UK land prices for the best part of two decades – he explains that land prices are based on a lot more than the productivity of the soil itself. "A number of factors go into determining the end sale price of a given piece of farmland. Obviously demand is the most significant, but so too is accessibility and location. Planning or development potential will also have an impact, as will people buying land as a business investment in order to shelter from inheritance tax."

Having witnessed the land market evolve throughout the most recent reforms of the CAP, Bailey is aware of its impact more than most. While he does accept that the SFP can represent a considerable subsidy for many farmers, he's not necessarily convinced that there has been a significant impact on the market since 2005. "Yes, land with entitlements tends to attract more interest because it represents a guaranteed return on your investment. However I don't believe the introduction of the single farm payment *per se* has led to an increase in farmers buying up more land."

Savills' own figures however may beg to differ. Figure 1 is a graph lifted directly from their *Agricultural Land Market Survey 2011*, illustrating the proportion of all buyers and sellers of land who are themselves farmers. As can be seen the proportion of "farmer-buyers" has *increased* by 26 percent from 2004 to

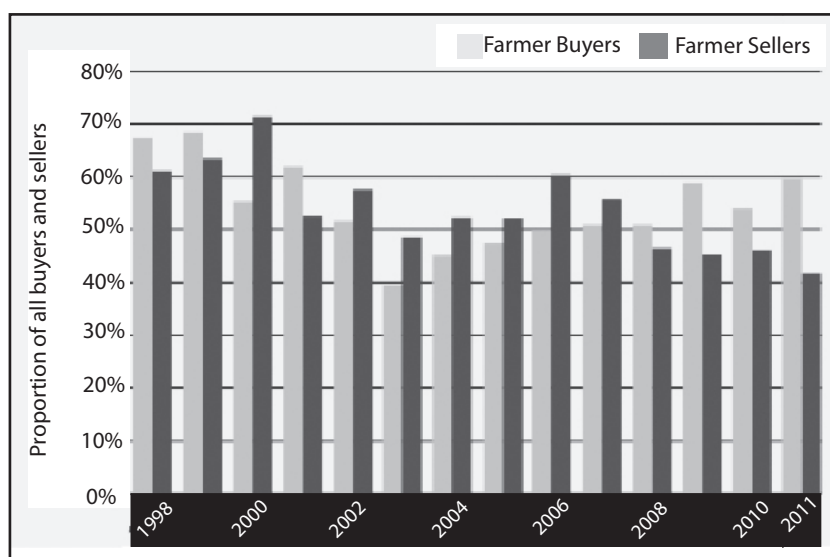


Figure 1 taken from Savills Land Market Survey 2011 illustrating a 26 percent increase in farmer-buyers in the market since 2004

2011, compared to a 25 percent *decrease* in the trend over the preceding seven years. The survey reports that "farmers represented 54% of all buyers in the eastern regions, 65% in the Western regions and 69% in the Northern regions including Scotland. The main reason for buying farmland was expansion, which was cited as the primary reason in 50% of all deals."⁸

Expanding the farm business seems like a pretty sensible reason for farmers to be buying more land. So sensible in fact that I struggled to imagine what could have possibly motivated the other 50 percent. "All sorts of reasons" replied Bailey, "The majority of these sales are farmers simply expanding their operations to make them more profitable, however some are rolling-over capital gained from other income, from sales and developments, and yes, investment of capital".

Bailey argues that such a trend can, reasonably, be excused as sound business practice by a growing number of farmers deciding to increase the size of their holdings. And while it's impossible to quantify the exact contribution of an individual's SFP cheques to the process, there is an uncanny correlation in the timing of this "farmland expansion" with the introduction of the Single Payment Scheme in 2005.

According to Defra's *Agriculture in the UK 2011* report total direct payments made to UK farmers under the SPS have increased by 13 percent since 2005, mirroring the rise seen in Figure 1. Over the same period the overall number of farm holdings in the UK has decreased by 11 percent with the greatest rate of decline (14.2 percent) seen in farms of 20-50 hectares. The only class which bucks the trend is farms of 100 hectares or more - which have increased their collective farmland area by 92,000 hectares since the SFP was introduced in 2005⁹.

While investment in farmland, using SFP money or not, may be dismissed by established farmers, it is at the new entrant end of the spectrum where its impact is amplified. Figure 2 is a graph lifted from the same Savills' report showing the average price of Grade 3 (medium quality) agricultural land over the past 20 years. The first half of the graph is consistent with the market inflation experienced throughout the second half of the 20th century, with an increase in land prices of 27 percent for the decade between 1994-2004. Since 2005 however, when the

SPS linked subsidy payments to farmland area, per acre land prices have risen by an average of £3,615, a whopping 181 percent.¹⁰

So how does Ian Bailey account for such a rise above inflation? “The land market is notoriously consistent – particularly in a time of recession when people are looking to safeguard their savings. That is really what we are seeing with the rate of increase in land prices over the past few years – which has been exacerbated by demand outstripping supply.” So – in a time of recession would he personally advise farmers to invest any savings they might have into more land? “Well yes – as an estate agent – I would certainly advise our clients to consider reinvesting in farmland.”

Land Capitalisation

The link between the introduction of the SFP and land consolidation was identified as early as 2008 by a handful of policy commentators as well as the European Commission themselves. The term “Land Capitalisation” was coined to describe the direct impact of the single payment system on farmland market prices. Alan Matthews, an agricultural economist and regular contributor to the *capreform.eu* blog explains how it works:

“Agricultural subsidies tend to be capitalised into the purchase and the rental price of agricultural land. Because of higher incomes farmers are prepared to bid more to rent or purchase extra land. But given that the overall supply of land is fixed, farmers will bid against each other up to the point where the entire increase in profitability is dissipated by the higher cost of land. Thus, it is landowners who are the main beneficiaries of farm support policies.”¹¹

Despite concerns raised by new entrants and small family farmers across Europe, it wasn't until 2010 that the European Parliament decided to investigate the impact of consolidation, and commissioned the Centre for European Policy Studies to compile a report. *EU Land Markets and the Common Agricultural Policy* evaluates the extent to which the introduction of the SPS has affected the capitalisation of land values – both sales and rental prices, as well as the distribution of farmland

within the current market.

The report's findings suggest that CAP subsidies have had an undeniable impact on land values, but it cautions that “the impact varies substantially across countries and appears relatively modest compared with other factors. Generally, the lower the land price, the higher is the impact of CAP policies.”

Referring to the UK specifically the report argues that: “Since 2004, better quality arable and livestock land has not grown at such rapid rates as poorer quality livestock and arable farmland. This is attributed to two factors: The first of these is an increase in demand by lifestyle buyers for poorer quality land. The second factor entails some effects of the shift to the SPS flat-rate scheme, making marginal land more attractive as an investment because the entitlement value is growing relatively faster than that for the better quality land.”

It goes on to conclude that: “Introduction of the SPS appears to have increased capitalisation in the least productive countries. The SPS seems to have put a floor on land values in Sweden and parts of the UK.” The report also highlights that the impact of CAP support is more significant on land rental prices as landowners are reluctant to enter into medium term lease agreements when policy is liable to change every few years¹².

Despite such a high level of recognition that land capitalisation is a real issue, its impacts appear all too easily dismissed as we enter the age of “sustainable intensification”. Wyn Grant is professor of economics at Warwick University and blogs at *commonagpolicy.blogspot.co.uk*. While he accepts that the SFP certainly has had an effect on the land market he argues that the consolidation of farmland is inevitable – regardless of the subsidy cheque: “The SFP does create an extra incentive to enter into farming because it can make the difference between running at a loss and running at a profit – but for farmers trying to make a living out of their farm without any other source of income, you simply have to have a larger and larger unit these days to secure economies of scale.”

He does however also acknowledge that the single payment system has, by its nature, had a negative impact on new entrants into farming. “With the previous system you had to produce in order to claim the subsidy, whereas now there is an assured

payment provided you keep the land in good heart. This is a big problem for new entrants and that's been exacerbated by the reduction in the number of county council farms – the real problem is trying to ensure there are routes into the industry for young people.”

The CAP Cartel

Faced with the findings of the *EU Land Markets* report, the latest round of CAP reform has proposed a remarkable solution for limiting the impact of the SFP on new entrants. Instead of an open incentive to actively get more young people onto the land the Commission has proposed a two percent “Young Farmer's Premium” on existing SPS entitlements. Quite how the Commission expects new entrants who don't have land, or entitlements, to benefit from such charity is anyone's guess

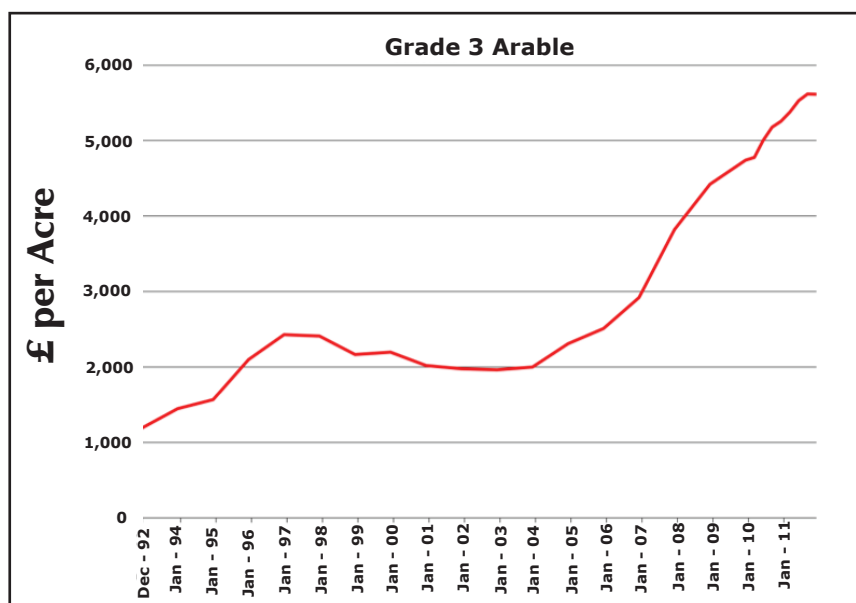


Figure 2, also taken from Savills Land Market Survey, illustrating a 181 percent increase in Grade 3 agricultural land prices since the SFP was introduced in 2005.

- but if adopted the Premium will only serve to subsidise a route into the industry for the children of farming families at the expense of those who are not.

It may be considered that land consolidation could be better targeted at the top by reining-in the ability of larger-scale farmers to exploit the single payment scheme and capitalise their annual cheque into new farmland. One effective solution which has been widely mooted is the proposed cap on the maximum SPS payment that could be claimed by any one individual or company.

The "Capping clause" was first proposed by an alliance of eastern EU member states seeking to stem a surge of foreign investment in their own farmland since 2005. As of December 2012 the proposed cap has been repeatedly revised upwards in an effort to get it past agribusiness lobbyists and now stands at an indulgent €300,000 a year. In SFP terms this equates to a single annual payment for a 950 hectare arable farm, which by anyone's reckoning should be approaching the kind of economies of scale championed by Wyn Grant. The National Farmers Union has been one of the most vociferous opponents to the proposal, stating "We believe that a cap on the largest single farm payments will have a disproportionate effect on UK farmers and contradicts calls for a modern, efficient farming sector."¹³

The UK has the highest concentration of landownership in Europe. The fact that a majority of the most powerful landowners vote conservative may explain the Prime Minister's personal reluctance to endorse the proposal. In its official response to the latest round of CAP negotiations the Government was in step, one could almost say synchronised, with the NFU: "The UK is opposed to the Commission's suggestion that direct payments to large farms should be capped. The CAP should encourage greater competitiveness, including by consolidation, which capping would discourage. This would be counterproductive to EU aims to develop a competitive agriculture sector."¹⁴

The bullish language of both the NFU and the Government belies an almost universal consensus that the CAP is making its final stand. Of a European budget of €110 billion a year the CAP devours €44 billion, a reality that cannot be maintained as the European Central Bank struggles to reverse a €34bn a year fiscal deficit¹⁵. As a result of the imminent restructuring of the EU budget the CAP will require an heroic cut in overall spending with few commentators expecting it to survive the next decade in any recognisable form.

As long as the CAP remains, however, it will continue to undermine itself because its key objective – uniformity – is so opposed to the diversity of its subject – agriculture. The consolidation of farmland facilitated by the single farm payment scheme is not the first time the CAP has rewarded the landed, at the expense of the landless, and nor will it be the last. But



When the CAP finally falls we may well see a return to the days when all farmers had to work bloody hard to make any living at all.

the audacity with which the single payment scheme created, at a stroke, a class of entitled individuals in 2005 is likely to go down in history as one of its greatest coups. And while a generation of new entrants may well suffer its consequences for decades to come, those of us now learning to farm without handouts are the ones who stand to gain when the CAP finally breathes its last.

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The photos accompanying this article were taken by James Ravilious in the mid Devon countryside in the 1960's and 70's.