RURAL AFFAIRS AND ENVIRONMENT COMMITTEE

FUTURE OF AGRICULTURAL SUPPORT IN SCOTLAND

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What should the direction of travel be for the future of agricultural support?

To answer this question first **stand back**, and ask what Scotland would look like without subsidy. What would be the negative results, from the point of view of Scottish society/ voters/ taxpayers? That might tell us where the support should go.

- My view, which many would disagree with, is that agriculture may not decline as much as expected after a phased removal of production subsidy. However, there would be a major shift in systems and in the geographic location of some types of production. Big losers would be activity in the hardest areas (the Highlands and Islands) and the input supply companies. This would also have some environmental impacts. Fewer farmers would derive all their income from farming.
- We generally make the mistake of judging the impact of subsidy by looking at the current situation i.e. the average beef and sheep unit makes no profit without subsidy. But this ignores the fact that markets are dynamic – the benefit of subsidy is lost over time as farmers compete for stock and land and inputs and build the value of the subsidy they receive into the price they pay. The removal of subsidy would be painful, but would change the cost structure.
- For an example, look at the change since the decoupling of subsidies (and ending of headage payments) in 2005. Ewe numbers in the Highlands and Islands have fallen sharply, but the output of lamb has fallen much less. The large numbers of small low value lambs are increasingly being replaced by fewer, heavier and better quality lambs. And the remaining ewes are producing more lambs per head.

What does all this mean, in my view, for the direction of support? In my short paper to the Pack inquiry I outlined the following principles.

Justification

We need a support system where support to farm businesses can be clearly and honestly justified. This is taxpayers' money and many taxpayers are in for a tough time over the next few years. It is legitimate for them to ask why on average farmers receive £25,000 of SFP per annum simply by filling in a form, while at the same time the local hospital is being squeezed by Government spending cuts. We in the industry can all argue that the SFP is simply a historical and transitional payment (the conversion of what was once price support under the intervention system, into a sum which can be more accurately distributed to producers, and which will no doubt be reformed into something very different after 2013), but that will not cut much ice with the urban masses. And it is very difficult to argue that this is a support to food production as most of it goes to low output businesses. Indeed the enterprises which can produce a lot of food per unit of input – for example pigs, poultry, potatoes – received no support. And it is difficult to argue that the SFP is a social support to guarantee all farmers a minimum level of income when for example, in my area of Aberdeenshire, 5% of the farmers get a third of the total SFP.

The Public Benefit or Public Goods criteria used in the justification of support under Pillar 2 are much maligned – they are sometimes difficult to define and to measure, and ignore what we as farmers tend to think is our obvious public good; food production. However, they give a clear and consistent way to show taxpayers what they are getting for their money. They are accepted by the World Trade Organisation and already protect and justify a huge level of support to rural areas, so we should grab them with both hands.

The historic basis of the SFP clearly is not justifiable in the long term. It was a good transitional measure. I would even defend many of those who cut production and still received the same level of SFP. They took rational decisions for their businesses. Their ability to continue receiving the SFP helped them speed up a restructuring which for many was inevitable in the long term anyway. This has helped the rest of the industry by getting supply and demand in balance. I could take you to businesses which have followed this route and have used the extra profitability to invest in old cottages and renewable energy and as a result are bringing much more into their rural economy than did the previous farming system. However, that transitional use of the SFP should come to an end in 2013 to be replaced by a much more justifiable support system.

Targeting

CAP funds are likely to be squeezed post 2013 and will decline steadily in real terms anyway. If the remaining support is to have any real impact it is inevitable that funds must be targeted where they are most needed/ will have the biggest return.

All the evidence suggests that many of the existing schemes are very poorly targeted. For example the LFASS is meant to assist farming in the most disadvantaged areas, but livestock are disappearing most rapidly from those areas.

Targeting is difficult for producers because it means redistribution, which everyone believes in as long as it doesn't affect them. However, better targeting means better justification of funding to agriculture as a whole and the likelihood that it can be retained for longer.

Market Focus
Production subsidies are lovely for the well established individual in the short term, but disastrous for the industry in the long term. During the period of large headage payments for suckler cows (since the 1992 MacSharry reforms), the unsubsidised margin from cows fell steadily, prices fell, the national calving percentage fell, Johnes, BVD and Leptospirosis became endemic, daily liveweight gains stagnated and total UK beef production actually fell. If anything the situation for sheep was worse. Many of us spent too much time on the numbers game, extensification games, heifer rule games and keeping cattle forever to get the second BSP. Now that subsidy is decoupled we find that the majority of the Scottish herd is unprofitable. The incremental improvements which every industry needs to keep ahead of the game did not happen while we were distracted, and the essential ongoing restructuring (poor performers getting out, good performers expanding) which is also critical to any industry did not happen to the required extent because quotas froze the structure.

This is not a popular view. However, I think the evidence (from around the world as well as the UK) and certainly my own experience, bare this out.

My experience since decoupling is that there has been an explosion of interest in breeding, disease management, EBVs, handling systems, reducing wintering costs, grassland management and producing for niche markets. If this continues we will see a revolution in growth rates and the numbers of stock which can be handled by one person over the next 15 years. Decoupling has given producers the freedom to look clearly at their enterprises.

The conclusion from our recent history must be that future support must not distort the business decisions of the entire industry – another argument for targeting of support only where it is most needed. Note that a production support such as a headage payment may be the best way to deliver the maintenance of activity which has local social and environmental knock-on benefits (e.g. cows on Tiree), but not across a large swath of the industry.

Capacity
Having rubbished universal production subsidies I am now going to defend a capacity to produce. The two are not incompatible.

Even if there is a massive world food shortage the UK and Europe would be among the last places to experience shortages, given our buying power. However, in a volatile world it makes sense to ensure that you have the capacity to produce more food if there is a real world crisis. I believe this should be one of the principles behind agricultural support policy, though in reality given the international nature of food chains this really needs to be coordinated at an EU level (if not higher). It would be massively expensive and economically disastrous for a food exporter like Scotland to try to maintain the capacity to produce the full range of foodstuffs, and by implication having every other country doing the same.

For me capacity does not mean maintaining the current number of cows or pigs or hectares of grain, or the current structure and location of enterprises. It means;

1. Maintaining the ability to produce. That means agricultural land quantity and quality, agricultural and business skills, a minimum agricultural research base, a knowledge transfer system which can turn the research into practical improvements, farm infrastructure (fencing, buildings, waste management), a strong animal and crop health system with targets to eliminate diseases, a flexible land tenure system and an overall legislative environment which is sympathetic to enterprise.

2. Understanding the reasons behind any downward trend and acting when there is a market failure and risk of total loss of capacity. In my view a good example would have been the pig sector if the conditions leading to its recent decline had continued and the survival of the single Scottish processor had been threatened. Many feel that the suckler cow and breeding ewe sectors are also in this position, but their financial position has improved sharply, there is a good argument that the reduction in numbers is part of an inevitable and essential restructuring which will leave the sector stronger, and while the red meat processing sector will find this very tough, most of the capacity will survive - though clearly the situation needs to be monitored.

The overall objective is to maintain a base which can react sufficiently quickly to the rise in prices which results from a food shortage.

This approach would not be justified for most industries. For example if UK car makers cannot compete in a free and fair market, Government should not try to prevent its demise. For a small number of industrial sectors – food, energy, perhaps defence – the consequences of not maintaining some national capacity may be too painful or strategically difficult in the wrong circumstances.

Of course there are huge problems in proposing the maintenance of “capacity” as a part of Scottish agricultural policy. It breaks just about every EU rule on production support, competition within the single market and unfair state aids. That’s why it really needs to be an EU wide policy, if it is to be a part of policy at all. The Scottish Government can have some impact on “capacity” in the way it implements policies which do fit EU rules. For example supporting hill cattle for environmental reasons and prioritising slurry storage grants for the pig sector has some indirect impact on Scotland’s production capacity. Article 68 gives a hint at policy moving toward more overt support for maintaining some capacity where it is fragile and where there are broader consequences for public benefits.

Simplicity
The Pillar 1 SFP is relatively easy for farmers to access and simple and cheap for our civil servants to administer. In contrast the Pillar 2 schemes, which must be much more tightly justified to meet public benefit criteria and to avoid competition law and state aid infringements, are more difficult to understand and potentially costly to administer. In some cases there is substantial “leakage” of funds to consultants and administration costs.

Clearly a balance may need to be struck between the justification and targeting principles outlined above and the accessibility of any support regime. The objectives of a support regime can only be achieved if the target producers take it up

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