Economic vs. Non-Economic Determinants of Diversification and Specialisation in Agriculture

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ABSTRACT

Empirical evidence from the sugar sector of the UK has revealed that farmers in this sector adjusted to the EU reform of the Sugar Regime either by diversifying production or by specialising in a small number of crops. This article hypothesises that these strategic choices were influenced by a number of economic and non-economic drivers. A probit analysis conducted with a sample of ex-sugar beet farmers was used to test this hypothesis. The result showed that only non-economic drivers (i.e., social-psychological variables) were significant in explaining the strategic choices made by the farmers. This suggests that traditional analyses based purely on economic considerations have to be considered with caution.

Keywords: Diversification, Economic Drivers, Multivariate Model, Non-Economic Drivers, Specialisation

1. INTRODUCTION

A number of important policy reforms of the Common Agricultural Policy (CAP) have been implemented by the European Union since 1993 with the objective of gaining economic efficiency in the rural sector and to meet with international commitments and demands of the World Trade Organization (Ridier & Jacquet, 2002). This new political orientation has in practice altered the business environment and farmers now operate in a much riskier environment because many crops are now exposed to the instability present in international markets (Sckokai & Moro, 2006; White & Dawson, 2005).

An example of this is the major reform of the CAP policies once used to protect the sugar sector that was implemented on 20\textsuperscript{th} February 2006. This reform is referred to as the Sugar Regime Reform (SRR). Following the implementation of this policy change, the sugar beet factory located in Allscott in the West Midlands region of the UK, where the ex-sugar beet farmers in this region (ESBF) used to commercialise their production before the SRR, was closed. As a consequence, the ESBF were obliged to reformulate their cropping choices in order to adapt to the new business scenario. The present research found that some of these farmers diversified their portfolio of crops in response...
to this reform by incorporating new crops of low profitability and low degree of risk such as oilseed rape and oats. In contrast, other farmers replaced sugar beet by increasing the area of land covered with existing crops. That is, they specialised in crops that they used to produce along with sugar beet before the reform.

This article proposes a novel multivariate model that considers economic and non-economic drivers explaining farmers’ strategic behaviour. The objective of this article is to use this model with the aim of identifying the most relevant drivers that explain the strategic choice made by the ESBF in response to the SRR.

The article is organised as follows. Section 2 provides a policy background of the CAP reforms and the SRR introduced by the EU. The aim is to show the policy context of the present investigation. Section 3 describes the proposed multivariate model. Section 4 shows the methods used in the investigation. Section 5 shows the results obtained in the empirical part of the research. Finally, Section 6 concludes the paper.

2. POLICY BACKGROUND

The Common Agricultural Policy (CAP) corresponds to a system of policy programmes and subsidies that the European Union applies to the agricultural sector. It has its roots in the Treaty of Rome signed in 1957 and its objective was to offer special treatment to the agricultural sector given the relative poverty of a large proportion of farmers in comparison with other sectors. In particular, this treatment included/aimed at the adoption of a long term policy of development based on the establishment of protective and administered prices. The general argument used to support the use of these prices was that food security had to be ensured by providing a minimum acceptable income to farmers in order to avoid the scarcity of food suffered by Europe during the Second World War (Gardner, 1996).

Throughout the years the CAP has been criticised for different reasons. Firstly, the associated costs of traditional policy programmes included in the CAP were very high (Gardner, 2001). Secondly, the application of these policies produced strong distorting effects on the economy (Marsh & Swanney, 1980). Finally, environmentalists argued that the application of CAP policies negatively affected the environment (Brassley, 1997).

In response to these criticisms, the Commission recognised that a radical reform of the CAP had to be introduced by means of the incorporation of a plan of development for the agricultural sector (European Commission 1992, p. 62). This plan materialised in a package of reforms known as the MacSharry reform (i.e., the first CAP reform), which were based on four main policy actions: price cuts to bring EU market prices closer to world prices; compensation for lower returns by area or headage payments; set-aside and extensification strategies to reduce production; and measures to improve the environment and encourage forestry (Brassley, 1997). Compensation was managed by means of new instruments called Compensatory Payments. These payments were direct income supports given to farmers to compensate them for losses of income arising from the reduction in price support programmes (Woldehanna et al., 2000). The objective of introducing these payments was to facilitate reforms of agricultural policies.

There is no doubt that the McSharry reform was an important first step towards a more liberalised system of support for the agricultural sector in Europe (Swinbank, 1996). However, its main objectives were not fully achieved. As a result, a new corrective reform referred to as Agenda 2000 (i.e., the second CAP reform) was developed (Gardner, 2001). This reform was built on the McSharry reform and focused on cutting intervention prices for cereals, beef, and dairy production; the use of compensatory payments linked to historic reference yields to compensate farmers for these cuts; and the use of a basic compulsory set-aside rate fixed at 10%. The Agenda 2000 reform was also supposed to help in stabilising the budget expenditure of the CAP which increased after the 1992 reform.

Both the MacSharry and Agenda 2000 reforms were innovative initiatives because
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