

An Analysis of the Capitalisation of CAP Payments into Land Rental Rates in Ireland

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Abstract:

In this paper the effect of decoupling on the capitalisation of agricultural subsidies into agricultural rents in Ireland are analysed using a dynamic rental equation estimated with a two step system GMM estimator that accounts for expectation error and endogenous regressors. The findings illustrate the importance of institutional details in determining the extent to which subsidies are capitalised. In the period prior to decoupling Pillar 1 subsidies were highly capitalised into Irish agricultural rents in both the short and the long run. Depending on the farm system considered between 67 to 90 cents per euro of subsidies were capitalised into agricultural rents. In the post decoupling period the rate at which Pillar 1 subsidies are capitalised into Irish agricultural rents is found to have declined. This change is likely due to the short term character of the Irish agricultural land rental market, where 11 month rental periods predominate, and the freedom that the 2003 reform of the CAP offered farmers to consolidate entitlements established on rented land. The generally very short term nature of Irish agricultural rental contracts offered farmers an opportunity to consolidate entitlements that is unlikely to have arisen in other Member States with agricultural land rental markets characterised by long term contracts. The results in both the pre and post decoupling periods highlight the high degree of inertia of agricultural rents in Ireland, and the importance of accounting for dynamics when investigating the capitalisation of agricultural subsidies into land rents. The high degree of inertia in rents means that the impact of previously capitalised agricultural policy persists through time.

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