

cases the options available can be used as an alternative to cropping, particularly on poorer soils or in awkward fields or corners difficult to cultivate economically.

PROFITABILITY STILL BEARISH

Despite the optimism on prices and the policy fronts, the outlook for profitability from producing crops, although better, is still not good enough for many producers. The results from Loam Farm (Andersons' 600 hectare example farm) for the two crop years, 2006 and 2007, are summarised in the table below:

Loam Farm Budgets £/Ha	2006	2007
Gross Margin	315	342
Overhead Costs	-256	-266
Pre Rent & Finance Margin	59	76
Rent & Finance	-134	-125
Drawings & Tax	-100	-100
Margin from Production	(175)	(149)
Single Payment & ELS	251	223
Margin after SP/ELS	76	74

Higher crop sales are likely to be partly offset by increased costs, particularly fertiliser, fuel and labour. Although margins from production should improve, they will still be negative after deducting rent, interest and drawings. Furthermore, although well run combinable crop businesses will still be profitable after bringing in the Single Payment and Entry Level payments, profits are likely to decline for the 2007 harvest because of the lower Single Payment.

CONCLUSION

Although price prospects for combinable crop production are improving, the Single Payment will still be needed to provide a profit after all costs, but the SP is expected to fall in the years up to 2012. Many arable businesses will therefore continue to look to other income streams – diversification, other jobs, land stewardship – to make a reasonable return from all their business assets. This sector is already the most diversified (largely through building rentals) and must continue to find opportunities – even more so if sugar beet is part of the rotation. Cost reductions through restructuring and on-going technical improvement will also be part of the solution. Andersons' consultants look forward to continuing to help businesses find the best mix of solutions for each situation.

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CHOICES FOR THE ARABLE FARM

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ARABLE BRIEF

INTRODUCTION

The price outlook for cereals and oilseeds is more promising than for several years. Furthermore, the Single Payment opens up opportunities to use business resources to seek profit in other ways if they are more rewarding than farming - the arable farmer can choose to crop fully, cut back or not to crop at all. This article provides some policy and price background against which to assess the realistic choices now available to an individual farm business.

PRICE PROSPECTS MORE BULLISH

World: global wheat stocks are forecast by the International Grains Council to fall this year, with wheat demand outstripping production by 12mt. Stocks are likely to fall below levels reached in 2003 which provided the platform for the price rally through into 2004. This does not mean that a price increase is inevitable, but it will make markets more sensitive to shocks such as droughts and localised shortages will provide price hot-spots.

UK: an annual soft wheat production of roughly 14.5mt is utilised for domestic purposes (human, industrial, animal feed and seed) with about 2.5mt exported. Exports appear small but it is this tonnage that sets the domestic wheat value, i.e. UK prices are set by 'export parity'. Forecasts suggest that the UK may change to prices set by 'import parity' rather than 'export parity'. Firstly, it is likely that UK production will continue to reduce in the coming years. In terms of consumption, there are several developments that are planned to increase usage from the 2007 harvest onwards:

- Cerestar, a starch and sweetener company with a facility in Manchester is switching from processing imported maize to UK wheat in a new plant under construction. With water frontage (Manchester Ship Canal), it is possible the company could import if prices dictate, but this is not planned. The facility will take up to 1mt of wheat when operating to capacity.
- Wessex Grain will shortly be constructing a bio-ethanol plant in Somerset. This will be capable of using 330,000 tonnes of UK wheat. Wessex Grain has indicated that once this facility is operational, another larger plant is planned further east.

This rise in UK wheat demand will not wipe out the exportable surplus totally unless more biofuel sites are developed. However, with a much lower exportable

surplus, the balance of export to import parity will become less distinct, quite possibly trading for greater parts of the year at import parity. This could potentially add up to £6-7 per tonne to domestic grain values.

Biofuels: The UK Government has now implemented a Renewable Transport Fuel Obligation (ReTFO). By 2010, 5% of all forecourt road transport fuel must come from renewable sources; in other words biofuel. Biofuel divides into biodiesel from vegetable oils such as oilseed rape, and bioethanol from wheat or sugarbeet. Several companies are developing biodiesel plants in the UK, notably in Teesside, Immingham and Merseyside. Wessex Grain will use wheat (see above), and British Sugar has begun modification to its plant at Wissington. It is unlikely that UK farmers will produce the raw materials to provide the whole 5% ReTFO requirement, but some contracts are already available, and this new demand world-wide is undoubtedly raising commodity prices.

Price Risk Management: UK futures prices are at their highest for 3 years. Futures values for wheat of over £85 per tonne for May 2008 have been available for those with storage. At these prices many producers can see a profit from production, and should at least be considering their risk management strategy.

POLICY MORE SETTLED

Once the Single Payment in England has settled down, farmers may be able to look forward to a period of less policy driven change in the period 2006-2012; apart from sugar beet growers.

- At the **WTO** level, the Doha Development Round does not look like concluding for some time yet and then any changes will be phased over several years. Longer term the EU will have to accept more market access for arable crops, and will have to stop export subsidies that will affect cereals. However the world market in the future is likely to be very different from now as pressures increase from population growth, eating habits, crops for energy and water utilisation.
- At **EU** level, there is no demand for further radical policy reform, but the recent Sugar Regime reforms will impact on English beet growers, and some changes to the cereal intervention system and even to set-aside may be imminent (see below).
- At **UK** level government can really only influence

Rural Development policy, and the main issue here for arable farmers is likely to be the level of modulation of the Single Payment and how much match-funding the Treasury will provide.

Sugar Reform: The reform of the sugar regime agreed in late 2005 will cut beet prices to farmers by at least a third by 2009. Compensation is designed to cushion the financial effect. However under the English regional average payment system the compensation will progressively be taken into the regional element of the Single Payment, so that by 2012 none will go exclusively to beet growers. Output will drop by around £600 per hectare so what had been a reliably profitable crop must now be more critically examined. Decisions on whether to produce will have to be taken depending on opportunities to increase yield and sharpen performance. It is likely that contract tonnage will continue to be met, albeit by fewer growers on a lower total area, and the level of collaboration within the sector must rise to meet the challenge of reducing production costs.

Cereal Intervention: The entry into the European Union of another two countries, Bulgaria and Romania, could provide additional pressure for change. Already, since the entry of the ten New Member States in May 2004, the tonnages in intervention stores have risen from 3mt to 18mt.

The main recommendation of a recent report is that intervention should be limited to one type of cereal (breadmaking wheat is suggested). Also that intervention should only be available in deficit regions (Portugal and Spain). The market would then be left to operate with surpluses flowing to deficit regions and substitutions between grain types. One side effect of changes in market support might be that **set-aside** is phased-out. Set-aside was originally introduced as a supply control tool. With decoupling of support under the Fischler Reforms there was little or no justification for keeping set-aside, and this anachronism may eventually be discarded.

Environmental Stewardship: The environmental schemes in England, Wales and Scotland are all likely to survive the changes to Rural Development Programmes currently being worked on for the 2007-2013 period. The Entry Level and Higher Level Schemes in England do provide arable farmers with the opportunity to reclaim modulation deducted from Single Payments. In some situations agri-environment options can be part of the rotation. In many