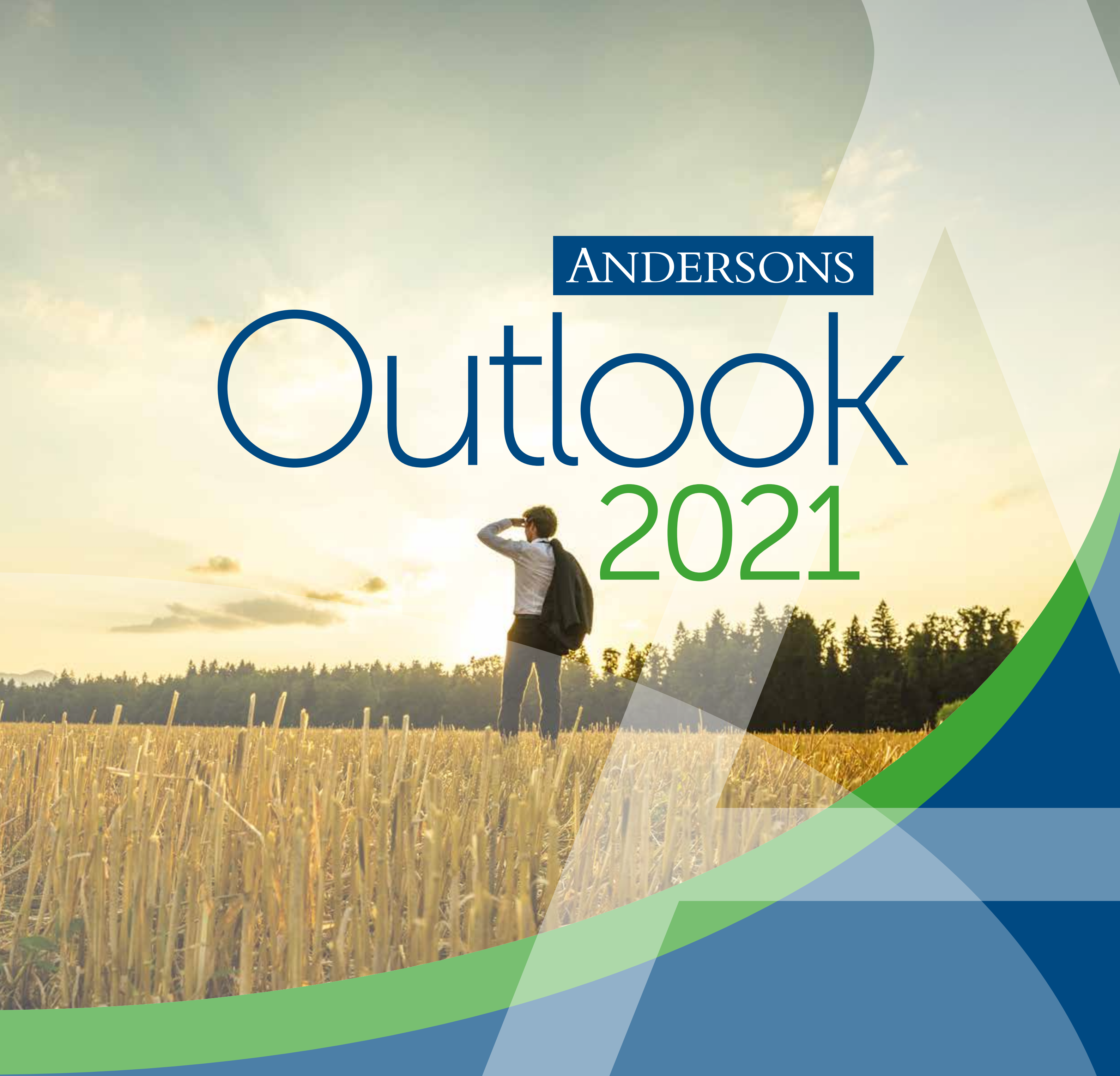
ANDERSONS

Outlook 2021



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Contents

Introduction to Outlook 2021 3

Farm Business Outlook
- Farm Profitability Prospects 4
- Economic Prospects 6
- Farm Policy 8
- Finance and Banking 11
- Land Prices and Rentals 13
- Topical Issue – Brexit and Global Trade 15

Cropping
- Combinable Cropping 18
- Potatoes and Beet 20
- Horticulture 22
- Topical Issue – Vertical Farming 24

Livestock
- Dairy 26
- Beef 28
- Sheep 30
- Pigs 33
- Poultry 35
- Topical Issue – Carbon and Net Zero 38

National Administrations
- Scotland 40
- Wales 42

Contributed Article
- Farm Woodland 44

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INTRODUCTION TO Outlook 2021

Welcome to Andersons Outlook 2021.

When the previous edition of Outlook was published a year ago, Covid-19 was simply a novel virus in an obscure corner of China. There was little indication that it would come to disrupt economies and lives in the way that it has. The UK farming and food sector has escaped relatively lightly – people always need to eat, and farmers are perhaps natural self-isolators! There have, however, been significant outbreaks further down the food processing chain. We hope all our readers have managed to stay safe and well during these unprecedented times. All being well, 2021 will see a return to some sort of normality.

Whilst it has taken a global pandemic to knock it off the front pages, Brexit remains a key issue for the agricultural industry. The politicians appear to have taken little notice of the production schedule of Andersons Outlook, and most of the articles in this publication have had to be written before the final result of the UK and EU trade talks are known. Even if a deal has been done, the 'friction' in trade between ourselves and our largest trading partner will be much greater – leading to higher costs, which may well be passed back down the supply chain. Whatever the trade outcome, 2021 will see the first year of the truly 'renationalised' farm policy outside of the Common Agricultural Policy. Although each part of the UK is doing its own thing and progressing at different speeds, the overall direction of travel is clear. In the future, there will be less support 'as of right', and land managers will be expected to deliver something to society in return for the funds they receive.

Andersons' consultants' experience is that this should not necessarily be something to be feared. There are still great opportunities to improve financial performance in all sectors of our industry. Without the distorting effects of direct support, there can be a greater focus on the areas of activity on farm that actually make a profit. Over time a stronger, more resilient industry should result, able to meet many of the other challenges that lie ahead.

We hope that you find Outlook 2021, written by members of all the Andersons' businesses, both informative and stimulating and, as ever, wish you all the best for a successful 2021.

John Pelham Nick Blake David Siddle Richard King
Directors, Andersons the Farm Business Consultants Limited

Farm Profitability Prospects

RICHARD KING

It is always quite foolhardy to try and predict farm profitability – the weather, commodity markets, exchange rates, and many other factors conspire to undermine even the best-constructed forecasts. For this edition of Outlook, further layers of uncertainty have been added with the effects of the global Covid-19 outbreak and the end of the Brexit Transition Period.

In terms of Covid, as documented elsewhere in Outlook, the effects on agriculture have been relatively limited. After a short period of upheaval when 'lockdown' was introduced, food markets soon regained their equilibrium. However, with the disease appearing to become chronic within society, and the economic fallout from this, there may be more fundamental shifts in food demand to come (see following article).

Brexit, and especially the Future Relationship (or not, as the case may be) between the UK and EU, is also discussed in detail elsewhere in this publication. The forecasts for farm profitability that follow are based on an 'orderly' Brexit with some sort of UK/EU Deal – even if it is minimalist and limited to preventing tariff barriers. Should there be no deal, then there will be winners and losers

> *Our calculations suggest returns [for 2020] will fall – by around 10% to £4.7bn.*

among the different sectors of UK agriculture. Overall though, returns in the industry are likely to be lower than those shown.

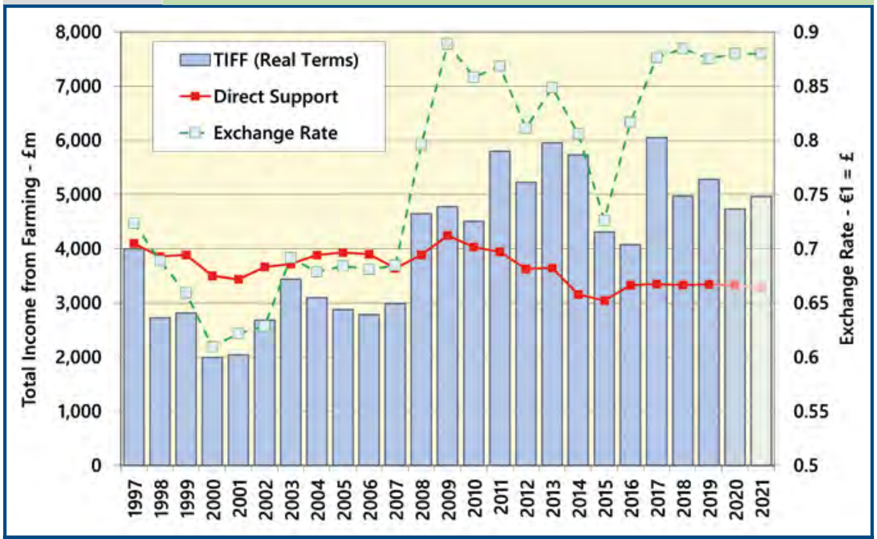
As usual, Defra's Total Income from Farming (TIFF) series is used to look at the profitability of UK agriculture. This has been running since 1973 (when we joined the EU) and shows the aggregate profit from all UK farming and horticultural businesses for the calendar year. In simplistic terms it is the profit of 'UK Farming Plc'. More precisely, it measures the return to all entrepreneurs in the industry for their management, labour and capital invested. Figure 1 shows TIFF going back to 1997.

The latest Defra figures relate to 2019. These show profits rising by 6% in real terms after the weather-affected 2018 year, to nearly £5.3bn. The data for 2020 and 2021 are based on a forecasting model run by Andersons – the first Defra forecast is usually made in December. Our calculations suggest returns will fall – by around 10% to £4.7bn. This is a consequence of lower crop output due to restricted autumn plantings in 2019, plus the effects of the market disruptions caused by Covid in the first half of the year. Whilst some costs have been lower (notably fuel), overheads generally keep rising.

The chart shows two other data series. The first, Direct Support, is a reminder of the level of public support going into farm businesses. It covers the BPS plus any agri-environment income. It can be seen that 'subsidy' has comprised perhaps two-thirds of farm profits in the last decade. There is a 'funding guarantee' that should maintain this until 2024 but, thereafter, amounts are likely to fall. Also, as payments move to a 'public goods' basis, there will be less profit in the receipt of subsidy as land managers will have to be doing something to earn it. These changes are still in the future. Exchange rate movements have an immediate effect and these are also shown on the chart. If there is a No Deal outcome this is likely to keep Sterling weak, which is generally good for farm profits (under normal

> *Any No Deal outcome would push profits down compared to 2020 – probably below £4bn, or even lower.*

Figure 1 **Total Income From Farming, Support and Currency - 1997 to 2021 (Real terms, 2019 prices)**



Source: Defra / Andersons

circumstances). If a Deal is done (even a limited one) the end of uncertainty should see the Pound strengthen. This can be seen as a regulating mechanism, perhaps preventing farm profits swinging too wildly in either direction whatever the Brexit outcome - although a No Deal is unlikely to be fully offset by currency shifts. For the purposes of forecasting TIFF, it is assumed the Pound stays in the range €1 = 85-90p.

Given the circumstances outlined above, the profitability prospects for 2021 look reasonably good. With more normal cropping conditions and Covid 'managed', profits would rise by 5%, close to £5bn – very much in line with recent years. But any No Deal outcome would push profits down compared to 2020 – probably below £4bn, or even lower.

Economic Prospects

GRAHAM REDMAN

In this section of Andersons' Outlook 2020, published a year ago, we made all the right predictions, but for all the wrong reasons. We talked about how the world was heading for global recession, how when the world gets sick, so does the UK (it was metaphorically referring to the economy). We also said unemployment would rise and productivity be poor. Nothing was mentioned about hiding from diseases, furlough and by quite how much the economy would shrink.

Perhaps, the UK was going to suffer anyway, and so the actions we took to avert the viral spread has had a smaller financial impact than they might have done. So many of us working from home have learned to be productive and, of course, farming has so far been largely unaffected.

But it will be. We can assume everybody with income or assets might be expected to help bail out the Government from the unprecedented debt it finds itself in. Short of default, Government debt is repaid by either economic growth; taxation which, for the 'have's', is presumably an inevitability at some point; and inflation, which erodes levels of debt as quickly as it erodes assets.

Briefly taking each individually, Government needs to encourage economic growth and quickly. This is hampered by ongoing restrictions and closures to retain a low 'R' number. The depressing state of not being able to mix freely with family and friends will presumably continue for some months until we learn to live with Covid-19 (and possibly Covid-20 and 21), as we do influenza. Office workers will remain Zoo(m) animals and agree deals with faces on screens. On paper, this is efficient, cutting out the niceties of asking how the journey was and polite coffee chatter, but in fact as much business is probably done in these peripheral events as the headline meeting. Trust is fostered, ideas are shared, and new acquaintances made. For the more physical work, rules of social distancing, cleansing, and covering-up will impact productivity.

> ***Taxes will presumably rise at some point but, currently, the debt has been financed by sales of Gilts at exceptionally low levels of interest.***

Less money sloshing about from fewer hospitality and hotel workers and other badly affected sectors will keep the whole economy from reaching the somewhat tardy 2019 levels probably for 5 years or more.

But new worlds also require new ideas, innovation and change, and the innovator and entrepreneur will do very well out of these unprecedented times, whether in agriculture or other sectors. Manufacturing (which includes farming) is a good way to get people back to work, albeit on lowish salaries; but blue-collar work also helps generate white collar, information-based (work from home) work too. This will be important with current projections of unemployment totalling 8.3% of the workforce after furloughing ends. Economic growth in 2021 should be the fastest this country has seen for decades at potentially 5% or 6%, but based on a shrinkage of 10% for the 2020 calendar year, will still leave us considerably poorer at Christmas 2021 than we were at Christmas 2019.

Taxes will presumably rise at some point but, currently, the debt has been created by sales of Gilts at exceptionally low levels of interest - for as much as 50 years in some cases, so the urgency to generate additional cash may not have hit the Chancellor of the Exchequer yet. Only if the fall in economic turnover reduces revenues beyond his ability to pay for our teachers, firemen, police, roadbuilders and, oh yes, some hospitals too, will taxes rise sooner.

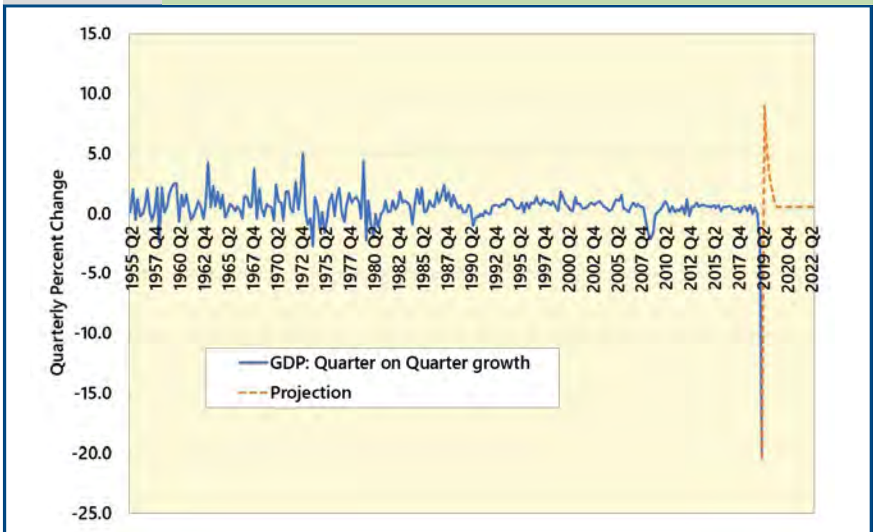
Inflation is low and probably will remain so in 2021 as the spare capacity in the workforce restrict wage rises. Deflation might be more of an economic risk. However, several factors should keep the UK from slipping into this spiral. Unprecedented levels of quantitative easing (printing money from thin air) is inflationary, Base Rates at their lowest for 320 years is inflationary and a weak Pound would be too. This last point is contingent on the outcome of the Brexit negotiations, but should a UK/EU deal not be done, then Sterling will probably be smaller than it was when this was written and that is inflationary (and this would also be good for farming short term too).

Will the outcome of Brexit, whichever way it goes, make any difference in the end to the economy? Well yes it will, but having had an economic body blow in 2020 of 10% of our GDP, it might just turn out to be only another 4% or 5% spread over a number of years, so it might not even get to the middle pages of the comments section, let alone the headlines. The Government might be able to swerve round the fallout from its enormous impact simply because we are fighting a Goliath, many times larger.

Whichever forecast we align ourselves with, the world, the UK and British farming has to emerge from Covid and other challenges in a decarbonised manner. This will leave economic opportunities for those prepared to embrace them but stifle the lifestyles of luddites and environmental rejectors not prepared to play their parts in removing carbon from their lives. We should consider the 2020's as the transition decade, and we are already 10% of our way through it. More opportunity beckons for the entrepreneur.

During a period of such intense change and upheaval, the entrepreneur will be favoured over those that passively wait for investment returns. When change is in the air, opportunity abounds for those light-footed and quick-thinking doers. Modern technology means few will harvest most unless policy prevents it. That is unlikely.

Figure 2 **UK Growth (Quarter-on-Quarter Change) – 1955 to 2022**



Source: ONS / Andersons

Farm Policy

CAROLINE INGAMELLS

We are entering a period of significant change in farm support. That said, all the devolved regions have announced the BPS will continue for 2021 although with some 'simplification' of the rules. Here we are already witnessing the expected divergence in legislation, as each region starts to write their own domestic farm policy post Brexit.

In England, all Greening requirements have been abolished from the 2021 scheme year; this includes Ecological Focus Areas (EFAs) and Crop Diversification (CD) – the two and three crop rule. But in Scotland, although CD will no longer be required, EFAs and the Permanent Pasture requirements have been maintained for 2021. In Wales, the Government has launched a consultation on a number of changes to the BPS, whilst it transitions to its new Sustainable Farming Scheme. Included in this are proposals to remove the Crop Diversification requirements for 2021 and move the EFAs and Permanent Pasture rules to the Cross-compliance Legislation. Further details of the Scottish and Welsh farm policy are included in the regional articles later in Outlook.

In England, the Basic Payment Scheme architecture may be continuing but, importantly, 2021 marks the start of the seven-year Agricultural Transition which will see direct payments reduced, so that by 2028 there will be no BPS-type of support.

At the time of writing (October 2020) only the payment deductions for 2021 were known. But it is expected that, by the time Outlook has been received by readers, Defra will have launched its long-awaited consultation on the Transition (originally expected in 2019). This will not only give us more of an idea of the deductions beyond 2021, but also further information on delinking of the BPS from land and lump sum payments.

> *All the devolved regions have announced the BPS will continue for 2021.*

Delinking is a mechanism that breaks the link between receiving support and occupying agricultural land. It looks very likely to happen, but it cannot commence before the 2022 claim year at the earliest. Once support is delinked a farmer could double the size of their holding or stop farming completely and they would still get the same future stream of income (tapering-off to 2027). It effectively gives the claiming business a right to the future support based on what the claimant received in a 'reference year' (or years). The key point is, the reference year could determine who gets the support through to 2027. The consultation should give further details on this.

Any Tenancy Agreements written pre-2019 are unlikely to have any clauses in them which deal with delinked payments. If a Tenant has made a BPS claim which included the reference year, the right to the future income stream would become vested in the Tenant. If the Agreement is brought to an end during the Agricultural Transition the Tenant would still have the right to receive the delinked income stream and the land may not have any 'support' for the incoming Tenant.

Lump-sum payments must not be confused or 'bundled-up' with delinking. It is the idea that the future stream of income from delinked payments is rolled-up into one single payment. But it is separate from delinking; it may not be introduced in 2022, it may not be available to everyone, it may not even be introduced at all. More information is (again) expected in the consultation. The idea is that it could be used as a retirement sum or allow for investments to be made. If it is introduced, it is unlikely to be available to everyone at the same time, as there just wouldn't be enough budget. There might be an age threshold for example.

As direct payments (BPS) are phased out, they will be replaced by payments for 'public goods' – services that agriculture can provide to society that are not delivered by the market. This will be through the much-publicised Environmental Land Management (ELM) scheme. Many of the objectives are familiar from previous agri-environment schemes, but elements such as climate change, air quality and hazard protection come more to the fore.

Defra is working with farmers to 'design, develop and trial' the new approach. At present, it is envisaged ELM will be based on a three-tier model;

- *Tier 1 – a broad (and shallow) offer available to all farms. Likely to have a menu of options and be managed online. It could look similar to the previous Entry-Level Stewardship (ELS).*
- *Tier 2 – this will require more intensive management from farmers. The focus will be on rewarding farmers for positive management such as biodiversity, flood management, carbon storage, landscape heritage etc. This will be the 'core' of ELM over the long-term. It will build on the current Countryside Stewardship.*
- *Tier 3 – this aims to get groups of landowners to work together to deliver widespread change or more complex change of land use, including afforestation, peatland restoration etc.*

2021 marks the start of the seven-year Agricultural Transition which will see direct payments reduced, so that by 2028 there will be no BPS-type of support.

In terms of timescale for ELM, the national Pilot Scheme is meant to open for Expressions of Interest (EOI) early in 2021 with applications commencing in April. Presumably, in order to express an interest, some details of the Pilot scheme will need to be published beforehand. This will at least give some indication of what ELM will look like in areas such as options, management requirements and payment levels.

In the interim, Defra has announced schemes will be in place as 'prototypes' for the three tiers which can be used as stepping-stones for farm businesses to transition to the new support landscape. A new Sustainable Farming Incentive (SFI) scheme will be the prototype for Tier 1. This scheme will not be available until 2022, but will be one which most farmers should be able enter. This is envisaged by Defra as a way for all farmers to recoup some of the BPS money which will be lost as we go through the Agricultural Transition. No details are available regarding the SFI scheme yet, but it is expected to cover areas that will be included in ELM, such as soil health and emissions, which are not well supported under CS.

Also in 2022 and 2023, the aim is to 'drive-up participation in the Countryside Stewardship'. The scheme will be simplified, and will be the stepping-stone to Tier 2 of ELMs. Ultimately Tier 2 of ELMs will depend on having a Land Management Plan for the farm which is expected to be drawn-up between the land manager and an accredited advisor. It is this element which will be tested under the ELM pilots in 2021. In the meantime, the current Countryside Stewardship will remain open in 2021 for 1st January 2022 agreement start dates.

In addition, the intention is also to roll out schemes, again in 2022-23,

which require more complex change of land use. These would form the prototype for Tier 3.

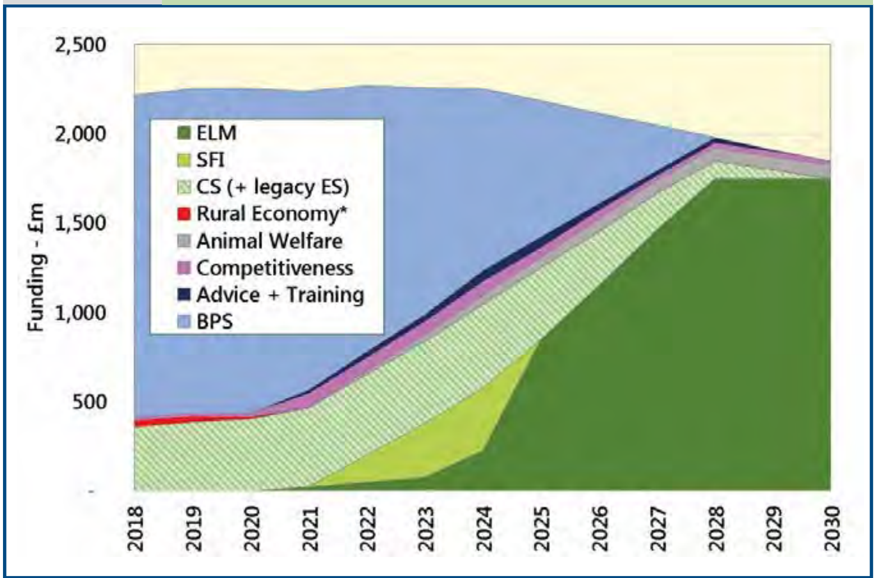
Whilst the majority of funding will be channelled through ELM once it is fully launched there will also be other support streams for farming in England, especially in the early years of the Agricultural Transition. These are likely to be in the following areas:

- *productivity improvements in farming, which may look much like the current Countryside Productivity Scheme*
- *a Future Farming Resilience scheme which will offer advice for farming businesses – especially to help with the loss of direct payments*
- *schemes for farmers to deliver animal welfare enhancements that go beyond the regulatory baseline*

It is unlikely that there will be a direct replacement for the EU Rural Development programme and the suite of schemes it funded. Funding for measures such as forestry, competitiveness and training are likely to come under the main 'agricultural' support system. But in terms of rural socio-economic development (i.e. a replacement for LEADER and the Growth Fund) this will be funded through the new Shared Prosperity Fund.

A new regime will be required to replace Cross-compliance, which becomes ineffective once the BPS is delinked from land. This is unlikely to see much of a reduction in the red-tape burden on farming, as much of Cross-compliance is already law. However, the way it is enforced (legal sanctions rather than BPS fines) and the administration of it (more proportionality and 'common sense'?) will be different. It also has linkages to ELM and animal welfare payments. These will only pay farmers for going beyond the 'regulatory baseline'. Where that baseline is set is therefore quite important.

Figure 3 **Possible English Agricultural Support Streams – 2018 to 2030**



** previous LEADER & Growth Fund grants* *Source: Andersons*

If the myriad of new support measures isn't enough, there will be changes to farm tenancy legislation through the Agriculture Bill. These are relatively minor though; the more contentious issues, which would allow Tenants to assign their tenancy to a third party on retirement or extending family members eligible for succession rights are being considered further. In addition, the Government is still reviewing responses to the consultation which proposes giving residential tenants more security – this could present problems for those renting out surplus farm properties.

The landmark Environment Bill is currently stuck in the Parliamentary process, but is expected to become law sometime in 2021. This will not only enshrine environmental principles in UK law for the first time, but also introduces measures to improve air & water quality and restore habitats. The Bill will see the creation of a new independent Office for Environmental Protection which will have the powers to hold the Government to account over its commitment to reach net zero emissions by 2050. The Government has also joined the international '30 by 30' campaign, a pledge that 30% of the UK's land will be protected by 2030. This will require a further 400,000 hectares of land to be designated and could see new National Parks being set up or existing areas extended.

Outlook 2020 gave a 'heads-up' on Defra's National Food Strategy. An interim 'Part 1' report has been produced which provides urgent recommendations to deal with the effects of Covid-19 and the end of the Brexit Transition period. But Part 2, due in 2021, is expected to make more sweeping recommendations on how systems should evolve to meet the future needs of society, impacting on the whole food chain.

As can be seen, Policy remains very busy as we move from the CAP to the post-Brexit landscape. There will be a period of quite intense change as businesses adjust to the new support schemes. But one thing looks certain, it won't be as simple as just claiming the BPS.

Finance and Banking

JAMIE MAYHEW

The past twelve months have been an incredibly testing time for UK farming both from poor weather conditions and the impact of Covid-19. Many banks closed their books for new lending due to the predicted negative impact Covid-19 would have on the economy. However now that they have reopened, there is a strong appetite for investment into 'UK Agriculture plc'.

As mentioned in last year's article, 'cash is king' – and this is even more true in challenging times. Businesses should always analyse the true cash position rather than focussing solely on the Profit & Loss figure. What is the cash position likely to be in your business on the back of 2020 and the impact on cash flow going forward? As a reminder, in order to analyse the true cash position of a business, one must take into account those costs that appear in Figure 4, the P&L.

Many businesses have taken advantage of the various Government schemes to soften the impact of Covid-19, however this does not mean that the problem has gone away; merely postponed. Coupled with the impact of the poor weather conditions affecting yields, businesses must plan their cash flow accordingly and where necessary begin conversations with lenders well in advance of any possible pinch points.

> *"There is a strong appetite for investment into 'UK Agriculture plc'."*

With the impending changes to agricultural policy, it is a known fact that subsidy levels are set to reduce. What is the cash generation of your business with the Basic Payment removed? In some cases, this figure will convert from a cash surplus to a deficit. Therefore, it is essential that businesses should use the time while these support payments are readily available to analyse the earning capacity and the total debt within the business and look to reinvest to become cash generative before subsidy. Perhaps the disposal of some assets could be used to repay existing debt or even to invest in new revenue streams.

There is a strong appetite from banks to invest in diversified income streams that can show a sensible payback term. With cheap money and changing consumer demand whether it be for staycations, desire to buy local foods, offices downsizing & moving out of towns/cities, new homes requiring storage and green energy, there is a plethora of opportunities provided that the new venture is in the right location. Although money is cheap at this current point in time, new lending should always be stress tested at a higher interest rate to ensure that the debt is affordable – 6% is the usual base rate figure used. Perhaps this is a good time to fix the interest rate while they are low which takes the risk out of fluctuating base rates. However, be mindful that some fixed

Figure 4 **Profit to Cash**

Profit/(Loss)
Add Back Depreciation (shown in the Profit and Loss account)
Add Machinery Sales
Add Capital Sales
Add HP Loan Income
Less Machinery Purchase
Less Capital Purchases
Less HP Loan Repayments
Less Bank Loan Repayments
Less Private Drawings
Less Tax Paid
Equals Cash Surplus/(Deficit)

rate loans come with hefty early repayment penalties should you wish to repay a lump sum.

Due to the various impacts UK agriculture faced in 2020, it is expected borrowings will increase over the coming 12 months. This could largely be to cover trading losses rather than new investment. With the upcoming uncertainties in the industry, now is the time to thoroughly evaluate your business to ensure that it is cash generative and in a strong enough position to withstand any potential downturns in profitability.

Figure 5 **Base Rates and Long-Term Borrowing Costs – 1998 to 2020**

Source: AMC / Andersons

Land Prices and Rents

GEORGE COOK

With so much change in the current business environment, let us take stock of the market fundamentals for land purchase and rental.

The rural land market is influenced by several underlying themes;

- *Land is a finite resource exposed to increasing and diverse demands*
- *Historic evidence confirms it is a safe long-term investment providing steady if not spectacular increases in value*
- *The non-monetary benefits of owning part of the countryside - buying into the rural idyll*

The latter has been given additional Covid-19 impetus. New arrivals will need to remember that the countryside is also a shop floor where people live and work. They will also have to grapple with the challenges of rural broadband.

In terms of the ever-broader range of demands on rural land area, this is illustrated by Mr Gove's concept of 'Public money for public goods'. For the majority of the time since the Second World War the main farm policies have focused on one service; the provision of food. This demand has been effectively delivered by the farming industry. It is now clear that the pursuit of these policies has come at the expense of some of the other 'eco-systems services' now coming to the fore, including:

- *Water quality*
- *Biodiversity above and below ground*
- *Loss of soil organic matter and the role of soil in climate change mitigation*
- *A range of other themes best summarised by the term 'Public well-being'*

> ***New arrivals will need to remember that the countryside is also a shop floor where people live and work.***

My reason for this foray in policy is because future income streams from Government will be driven by delivery of outputs linked to these themes. These will form the backdrop to the new Environmental Land Management (ELM) scheme. The shift from area based to outcome-based income streams will in turn have an impact on both land and rental values. In time it is likely to require a closer working relationship between landowner and manager to optimise returns to both. Whether that is to design a scheme for creating wildlife corridors, habitats or nesting sites or whether it is the potentially exciting opportunities offered for carbon sequestration; collaboration between landowner(s) and tenants will all be important.

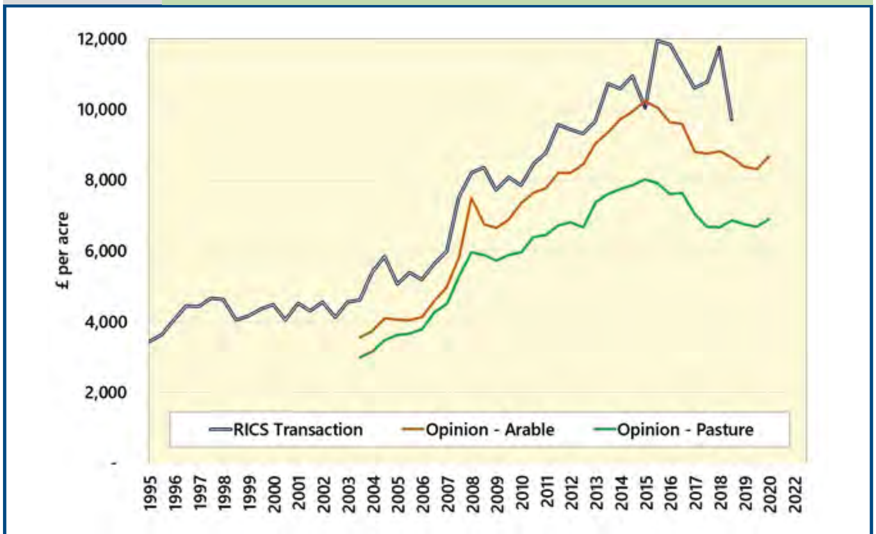
In terms of current land prices, Figure 6 shows average values for England and Wales. Unfortunately, good data on land prices is becoming ever-harder to obtain. The benchmark RAU/RICS series has been suspended since 2018. The figures shown thereafter are Andersons' figures, based on an 'index of indices' from national Land Agents' figures.

These figures mask significant regional and intra-regional differences where local markets can be driven by two or three individuals with significant surplus funds.

Following a period of decline since 2015, the latest figures suggest there has been an 'uptick' in values. This may be linked with the general increase in property prices since the lockdown eased.

Looking to the future, we would expect neither boom nor bust in land values. General economic uncertainty and affordability issues

Figure 6 **England & Wales Land Prices (Real Terms) – 1995 to 2020**



Source: RAU / RICS /Andersons

> ***The shift from the area based to outcome-based income streams will in turn have an impact on both land and rental values.***

will be bearish factors. As discussed in a previous article, the phase-out of direct payments will also be a negative – albeit support has a relatively small influence on capital values.

Of more importance are the capital tax advantages of owning land. There are almost constant concerns that reliefs under Inheritance Tax (IHT) and Capital Gains Tax (CGT) will be amended to the detriment of landowners – even more so in the current climate when the Chancellor has a big fiscal hole to fill. However, we would be surprised if there are any significant changes in the short term – both IHT and CGT are pretty 'small beer' when it comes to raising revenue and the Government has larger issues to worry about.

With borrowing costs remaining low (see previous article) and the underlying demand for land continuing, all these factors may, to a large extent, cancel each other out and values will remain stable through 2021.

Turning to rental values, rents under the old AHA Tenancies remain driven by the earning capacity of the holding. I foresee some interesting discussions and arbitration decisions around the concept of delinked payments and the subsequent reduction of land-based income. Once ELM is in place, there could well be some further fascinating negotiations between Landlord, Tenant and their respective agents when assessing the earning potential of the holding; what ELM income should be included in the calculation? – what the Tenant chooses to sign up to, or what the Landlord considers to be the 'best' scheme for the farm?

Short term, I expect there to be little change in local rental markets with the current Mexican stand-off in Landlord and Tenant persisting in relation to the serving of notices.

It is hoped there is an element of common sense and a practical approach remains throughout this process.

Moving onto FBTs – standard methods of calculation of the rent being the Basic Payment plus an amount – with that amount being determined by the Tenant based on what they think they can earn from cropping the holding.

Landlords and their agents tend to go for the highest open market rent tendered, which on occasion has left the land at the end of the agreement in a worse condition than at the start.

Furthermore, the withdrawal of the area-based payment is likely to make the calculation of rent more challenging, not least because Landlord and Tenant may have differing views on the optimising of income on the holding. Both parties will therefore need to be very clear on their objectives to enable a meaningful discussion to take place. This will need to strike a balance between:

- *optimising income on the most productive land on the holding through farming!*
- *enhancing and optimising income from the new income streams from ELM and other possible schemes once the details finally become clear.*

To this point I have managed to avoid the 'B' word – but Tenants will need to be careful how they do their calculations and be mindful of the terms of any trade deal with Europe and beyond.

Topical Issue- **Brexit and Global Trade**

MICHAEL HAVERTY

> ***Irrespective of the [UK/EU] future relationship negotiations, there will be significant changes to how UK-EU cross-border trade will operate.***

At the time of writing (mid-October), the UK-EU negotiations are reaching yet another climax. Unfortunately, publication deadlines prevent us from analysing whichever outcome of 'Deal' or 'No Deal' emerges. However, with the Transition Period ending in December, irrespective of the future relationship negotiations, there will be significant changes to how UK-EU cross-border trade will operate. Furthermore, the UK is also negotiating trade deals with several other countries and these could arguably have as much, if not more, of an impact on the future competitiveness of UK agri-food. With this in mind, it is worth looking at British farming in a global context.

Figure 7 shows that the UK is wealthy, densely-populated and trades freely, but also emits a lot of greenhouse gasses (GHG). British agriculture is pretty insignificant on a global scale apart from niche segments such as lamb production. Whilst the UK will be keen to do trade deals, farming is unlikely to be prioritised. With a 3.3% share of global GDP, the UK's bargaining power will be limited versus the likes of the US, which has a 25% share of global GDP. This is crucial regarding standards, as the US is likely to insist on its measures being the basis for trade under a US-UK trade deal. This, of course, is a major point of contention between the farming industry and the UK Government – highlighted during the passage of the Agriculture Bill through Parliament.

The question of standards, and a level-playing field for UK producers is especially relevant for products of animal origin, particularly, meat. To demonstrate this, Figure 8 on the next page compares the UK (GB) beef price with selected international competitors. Brazil, being the lowest-cost major producer, effectively sets the world market price. In recent years, it has been substantially below the GB price (often more than £1 per kg lower). The imposition of the proposed UK Global Tariff (UKGT) would safeguard the competitive position of British producers from Brazilian imports in the short-term. However, if future trade deals allow significant volumes of Brazilian beef into the UK at low or zero tariff levels, then UK producers

Figure 7 **'Global' Britain's Agricultural Sector**

(2018 data unles stated)	**UK**	**World**	**UK%**	**EU%**
Population (billion)	66.5	7,594.3	0.9%	5.8%
Agricultural Land Area (mHa)	17.8	4,86.3.3	0.4%	3.7%
GDP ($tr)	2.9	85.9	3.3%	21.8%
GHG Emissions (mtCO_2e) (2017)	546	45,261	1.2%	8.1%
Agricultural Trade ($bn)	70①/32②	1,749	4%/1.8%	2.7%/2.7%
Cereals Production (mt)	21.1	2,962.9	0.7%	9.3%
Milk Production (mt)	15.3	683.2	2.2%	22%
Beef Production ('000t)	922	67,354	1.4%	10.4%
Lamb Production ('000t)	298	9,498	3.1%	5.8%

Sources: World Bank / OECD / FAO / WRI / Andersons ①imports /②exports would be severely undermined. The chart also shows that if US producers gain access to the UK market via an FTA, they will also be very competitive.

Having a 'level playing field' is a frequently quoted concept in the UK-EU negotiations. This principle should equally hold elsewhere with respect to the standards that British producers must adhere to vis-à-vis their global counterparts. A baseline encompassing food safety, environmental protection and, animal welfare is needed, below which, the UK will not go in terms of acceptance of imports. This baseline needs to be set so that British farmers can be competitive whilst safeguarding their hard-fought reputation as quality food producers. Only then, can UK farming be best-positioned to exploit the opportunities ahead in terms of maximising domestic sales, protecting its share of EU markets and exploiting key export markets with its quality food value proposition.

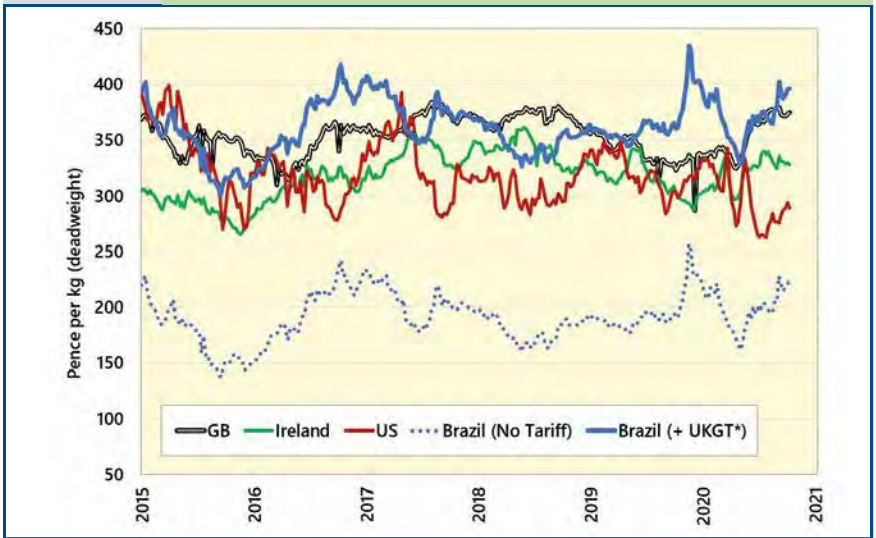
Turning to the more immediate UK-EU talks, it seems likely that any trade deal struck will be quite basic, given the time constraints. For agri-food, this is set to comprise of a basic zero-tariff, zero-quota Free-Trade Agreement (FTA). Whilst this means trade might be 'free' in terms of no import tariffs or quota restrictions, future trade would still be subject to significant non-tariff requirements. In last year's Outlook, Non-Tariff Measure (NTM) costs were examined in detail. Under an FTA these are estimated to range from 1-3% for red meat; 5-8% for poultry meat (as it is lower priced); 5% or less for dairy and horticultural produce; and for bulk cereal and sugar shipments are minimal (<0.1%).

For exports to the EU (and trade from GB to NI) these costs will apply from the start of January – whether there is a Deal or not. Importers to the UK will have a limited 'grace period' with the UK Border Operating Model seeing some checks delayed until July 2021. Many businesses have been dealing with the Covid crisis and have been waiting (and waiting) for the outcome of UK-EU negotiations. Therefore, preparation time has been woefully inadequate. This needs to be recognised, with an 'implementation period' for at least six months from January to allow businesses time to adjust. Such periods are often a feature of other FTAs.

Businesses still need to do what they can to help themselves and prepare for the regulatory changes ahead. These are significant. At present, those wanting to trade food products into France, for example, simply have to complete the commercial documentation and, as long as the products are approved for sale in Britain, they are automatically approved for export to France. From January, as set out in Figure 9, a business will be required to have a number of 'registrations' and then follow 11 (at the time of writing) steps. These cover areas such as VAT arrangements, export health certification, customs declarations as well as the applicable Safety & Security declarations. Teething problems seem inevitable.

Trade between GB and NI will also be affected. Shipments into Northern Ireland will require additional documentation relating to customs, safety & security and sanitary and phytosanitary (SPS) checks. In the event of a No Deal, the import duties could be applied and firms will also have to account for VAT. The 'red-tape' requirements for goods being shipped from NI to GB are still unclear, although the UK Government has pledged 'unfettered access'. As NI will be de-facto participating in the EU Single Market, regulatory barriers from NI to continental EU (EU-26) are expected to be minimal. This could potentially create opportunities (e.g. for lamb exports) vis-à-vis GB producers if

Figure 8 **UK and Selected International Beef Prices – 2015 to 2020**



Source: Bord Bia and Andersons

> ***It seems likely that any trade deal struck will be quite basic, given the time constraints.***

there are frictions on GB-EU trade.

By the time Outlook 2022 is published the situation with UK-EU trade should have become clearer (Haven't we heard this before? – Ed). The next year could see some upheaval as the sector adjusts to the new arrangements. But trade policy will be an ongoing issue for farming in the post-Brexit era and new threats and opportunities will be presented as deals with countries around the world are progressed. In this sense, Brexit will be more of a process than an event.

Figure 9 **Regulatory Steps on Agri-Food Exports from GB to France Post-Transition**

Stakeholder	Steps Involved
Pre-Requisites	• Economic Operator Registration & Identification (EORI) No (import/export license) • EU approval for both GB (exporting country) and the dispatch plant. • FR Importer registered with French authorities importing animal origin products.
GB Exporter	1. Zero rates VAT (Goods leaving UK); creates commercial documentation (invoices etc.). 2. Organises export health certification (via APHA). 3. Arrange Export Accompanying Document (EAD) export declaration.
HMRC	4. Use EAD to auto-generate an Exit Safety & Security Declaration (EXS). 5. Master Reference Number (MRN) generated by EAD/EXS lodged on Goods Vehicle Movement Service (GVMS) which then creates a Goods Movement Reference (GMR).
Haulier/ Freight Forwarder	6. Obtains GMR (needed at Border Control Post (BCP)), where regulatory checks will take place (Documentary, Identity, Physical Checks etc.), and transports the load.
French Importer	7. Creates a TRACES NT (required for SPS goods); arranges import pre-entry lodgement. 8. Books the BCP (e.g. Calais) if load contains SPS goods. 9. ENS Entry Safety & Security declaration needed 2hrs before goods arrive at FR port. 10. Pays import duty to French Customs or to agent (if agent uses deferment account). 11. Accounts for FR VAT either payable at border or through VAT accounting (if available).

Source: Customs Clearance Consortium and Andersons

Combinable Cropping

SEBASTIAN GRAFF-BAKER AND JOE SCARRATT

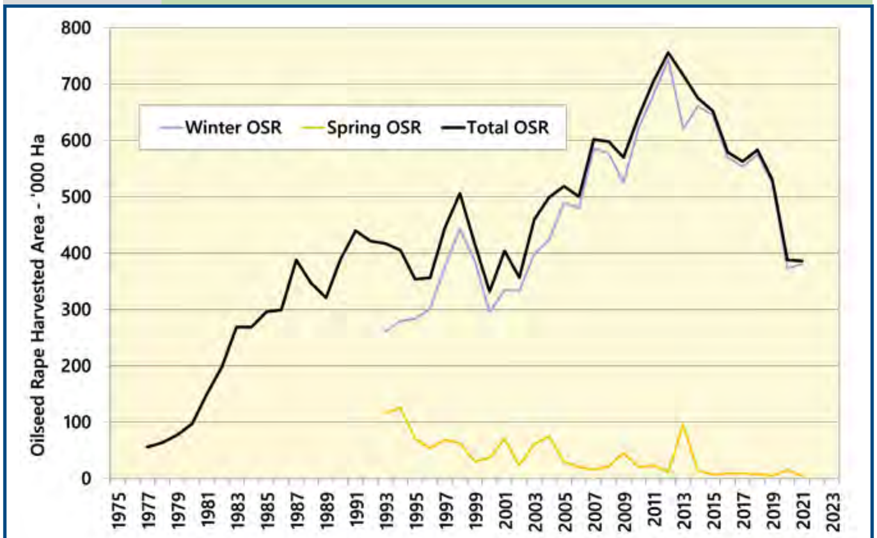
2020 has been a challenging year for all in the cereals sector, mainly determined by the lack of autumn sowing in 2019. The very dry weather following the planting of spring crops only compounded the worry, which for some has led to financial results many would rather forget. However, for others, harvest was not as bad as they had envisaged and, combined with a buoyant marketplace, it will not be the disaster first feared.

2020 will see the end of oilseed rape on many farms. The dry period during establishment in 2019 combined with relentless Cabbage Stem Flea Beetle (CSFB) pressure led to some very poor results at harvest. As a result, suggestions are that crop areas for 2021 harvest could be below 400,000 hectares, albeit the amount written off could be less than the last couple of seasons due to better establishment this autumn. Whilst we have seen this coming slowly for a number of years, it really is a game-changer on many arable farms. Crop area figures show it has been a mainstay crop for many farms since the late 1980's.

Despite its inherent high cost base and other challenges, oilseed rape has been the most profitable break crop on many farms, as well as helping to spread harvest workload with an early start. Pulses have well known benefits to following cereals and many have achieved good results with peas and beans in 2020, but their yield remains variable and there is thus a risk associated with large areas. Oats have a growing market on their side but only spring crops fit grass-weed situations and spring varieties are less favoured by the end user. Linseed will inevitably spark interest again, with some trying winter crops as a direct replacement for oilseed rape with early sowing and harvesting. Other options might exist in mixed farming areas with forage crops and/or re-introducing livestock when working with others with the specialist skills and knowledge.

With alternative break crop gross margins of £200-245 per Ha less than OSR, the obvious choice for many is to extend the rotation to include a greater proportion of cereals. This effectively reduces the break crop area to minimise the effect of simply replacing OSR with a less profitable alternative. On heavy soils, the most profitable (and sustainable) rotation will be two wheats after a break crop, followed by spring barley. Others may even return to continuous wheat / cereals.

Figure 10 **UK Oilseed Rape Area – 1975 to 2021**



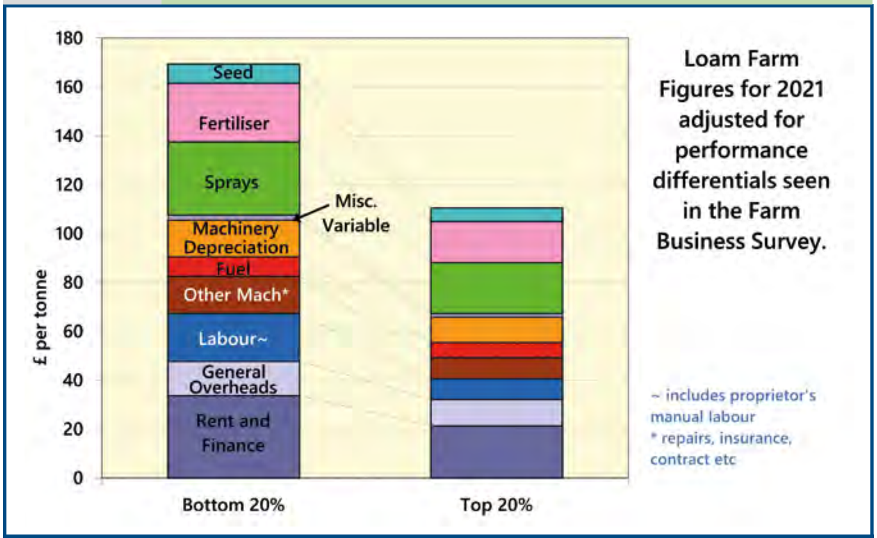
Source: Defra / Andersons

It is perhaps more challenging on lighter soils where second cereals tend not to perform so well. The key to minimising the financial impact is to look at the gross margin across the whole rotation rather than direct crop replacements.

One point the industry has now started to realise, as a result of the unique circumstances of 2020, is that spring cropping is perhaps not as 'dreadful' as many first feared. Clearly, if you simply compare gross margins, in most cases there is a negative financial impact compared to winter wheat / autumn cropping. Businesses need to build on the opportunity to consider their overhead cost structure (machinery and labour costs) in light of spring options; the flattening of work peaks reduces the need for overall capacity (machine sizes, horse-power, seasonal labour etc). As such, net margin comparisons could be more attractive. This is even more pertinent where businesses may be considering whole-field stewardship options as one of their replacement break crop alternatives. AB15 two-year legume fallow is an example of an option under the current English Countryside Stewardship which may, in some situations, act as the break crop. Given the five year term of such agreements (and potentially longer if rolled into ELM), businesses must make the hard decision to cut capacity (and thus cost) in the machinery and labour fleet to make sure there are positive financial benefits. Comparing gross margins is only part of the story with the medium-to-long-term commitments such schemes give. There is an ability to de-risk businesses and improve margins.

As a general rule, this will only work for average performers, or poorer land, where the risk vs reward ratio remains higher. For top performers, and good soils,

Figure 11 **Range in Wheat Cost of Production – Harvest 2021**

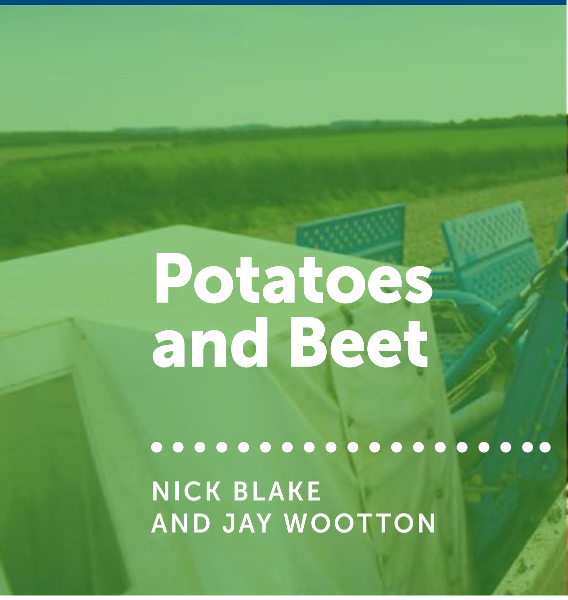


Source: FBS / Andersons

> ***The end of oilseed rape ... is really a game-changer on many arable farms.***

continuing with 'full' cropping is likely to be the best way forward. Productivity remains one of the key differences between business performance, certainly not scale. It is simply understanding land capability and having excellent attention to detail. Scale and the balance between proprietors vs employees can make a key difference; incentivisation and good management is essential to deliver top quartile returns. These are often the result of multiple small improvements which when combined deliver large changes to the bottom line. Productivity remains the basic principle if businesses are to thrive. Cropping poor land offers low returns and more importantly is high risk.

The changing support system (in England at least) means there is likely to be a significant shift in incentives over the next decade. The BPS will no longer be there to maintain farm incomes from land where, to date, some businesses have elected to grow combinable crops on poorer areas and incur losses, albeit hidden. Support is already targeted at land uses such as growing food for wildlife and the permanent removal of carbon dioxide from the atmosphere (Woodland Carbon Guarantee Scheme). It is expected that support will be further targeted at such land uses. Combinable cropping will remain a key enterprise where land selection and the application of resources (particularly labour and machinery) can create profits without subsidy. But many businesses may need to be both more selective in what land they elect to use for combinable crops and also more broad ranging in their overall land use. Those that start planning for this now, are most likely to create profits from both growing crops and collecting subsidy and therefore successfully navigate through the next 5-7 years of uncertainty.



Potatoes and Beet

NICK BLAKE
AND JAY WOOTTON

Potatoes

At the time of writing, the AHDB planting report forecasts the 3rd lowest GB potato area on record. Had the impact of Covid-19 become apparent any later in the planting season, it is likely that plantings would have been closer to 'average', creating further challenges around supply and demand.

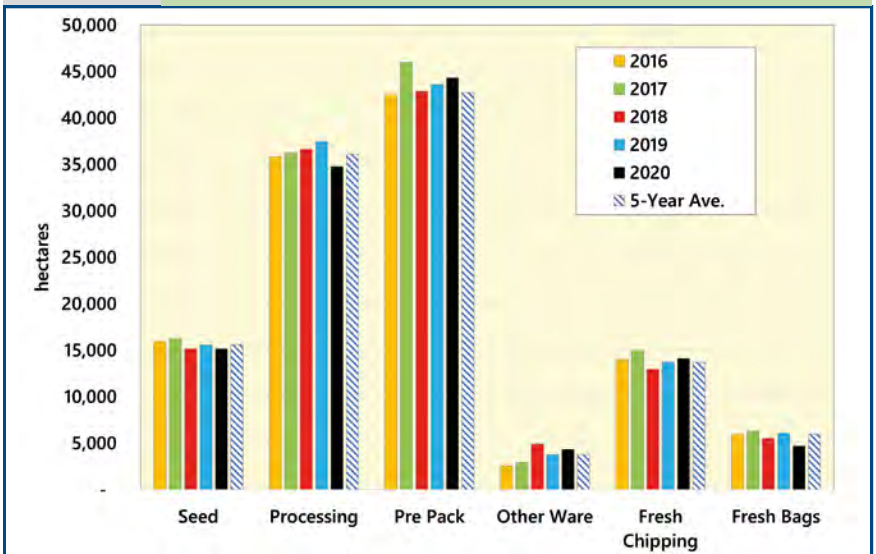
The quick reaction of the processing industry to the pandemic will have certainly helped underwrite the 2020 market, although the season continues to be a challenge so far. According to the AHDB there was a reduction in processing area of 7.1% as the intended market, and an increase in packing area of 1.6%. This looks to be a reaction to a lack of processing demand at the point of planting.

The further Covid-19 related impact on the 2020 market remains to be seen, but it is likely that there will be more than adequate supply in the marketplace. Quality issues are also apparent, with Wireworm problems being seen in a number of packing and processing crops. The loss of Mocap will have exacerbated this issue. Site selection will have to be even more carefully considered, with no alternative methods of control. Another agronomic challenge for 2021 will be the efficacy of storage regimes to manage sprout control, with the 2020 crop being the first storage season without CIPC.

The range in cost of irrigation is becoming wider, and increasingly this is not being recognised where the services are provided.

In the last Outlook we commented on the move towards increased irrigation in the UK potato sector. In our experience, the range in cost of irrigation is becoming

Figure 12 **GB Planted Area By Sector – 2016 to 2019**



Source: AHDB

wider, and increasingly this is not being recognised where the services are provided. The average charge for irrigation is still around the £100 per Ha for an application of water which includes the labour, infrastructure, energy and water cost itself. The actual cost can vary significantly depending on the following:

- ***Cost of water*** *– supported or unsupported supply, winter or summer abstraction, reservoir or surface water.*
- ***Type of infrastructure*** *– fully automated pressurised plastic lined reservoir with hydrants every 72 metres, versus Internal Drainage Board drains, and a diesel pump located adjacent to the reel. Booms versus rain guns.*
- ***Labour*** *– irrigation labour (employed for the season regardless), versus full time staff moving irrigators amongst other jobs.*
- ***Energy*** *– old diesel pumps versus invertor driven energy efficient electric pumps.*

Often many of the above costs have been incurred, regardless of the amount of water applied.

Before the season is upon us again, consider the actual costs (both fixed and variable) of irrigation within your own business.

The availability and responsible use of water will continue to be important in all forms of agriculture. As this article is written, there is news of a new water futures trading option in the US. This could signal the future management of this resource in the UK too.

Sugar Beet

This time last year we noted that sugar appeared to be in a better position than other commodities in the event of a No Deal Brexit, and lack of self-sufficiency in sugar production presented an opportunity for the industry. Since then, the Government has announced a proposed Autonomous Tariff Quota (ATQ) for 260,000 tonnes of raw sugar. This volume would be allowed into the UK market without paying the new UK import tariff of £280 per tonne. Depending on how this is implemented, it could mean an increase in cheaper imports which are likely to leave UK beet sugar production uncompetitive in the market place. This would jeopardise the viability of UK sugar production.

The loss of neonicotinoid seed dressings has resulted in crops appearing to be adversely affected by Virus Yellows. Combined with a difficult Spring and late crop establishment, the yield for 2020 is likely to be disappointing for many. The trade-off between harnessing potential yield from the sugar beet crop, and protecting the prospects of the following crop will need to be considered in the context of soil type, rotation, infrastructure, and approach to delivery.

> ***The [beet] yield for 2020 is likely to be disappointing for many.***

The guaranteed minimum price for the 2021 contracts remain unchanged from the previous year. The headlines of the Virus Yellow compensation scheme of £12m are eye catching, but the detail requires scrutiny, and at the time of writing much of this was unconfirmed.

A pilot scheme for growers to take responsibility for marketing a small proportion of their own crop through Czarnikow Group is an interesting concept, and we look forward to more details on the results of this initiative.

Horticulture

JOHN PELHAM

Whilst some horticultural crops are highly mechanised (e.g. vining peas and carrots), many have a significant seasonal labour requirement for crop establishment, husbandry and harvesting. For some crops this can represent as much as 70% of all expenditure. Because of the volume, range and complexity of tasks, mechanisation is less developed than for, say, more widely-grown crops such as cereals. By way of illustration, the labour cost for wheat production is typically in the range £80-150 per hectare; the equivalent for strawberry production is £40,000-70,000 per hectare.

Covid-19 has presented a significant practical challenge to those with seasonal workforces, which has inevitably led to increased employment costs for the 2020 season; in some cases by up to 15%. However, it is the twin issues of labour cost and availability that have, and will, dominate horticultural economics and, therefore, production in 2021 and beyond.

Since 1999 seasonal wage rates have been set by the National Minimum Wage and, from April 2016, the National Living Wage. It was the introduction of the latter, with a target rate at 60%

> *For some crops labour can represent as much as 70% of all expenditure.*

of median earnings, which has led to unprecedented wage cost inflation. In the last five years the hourly rate has increased by some 35%, with severe financial implications for those businesses for whom employment is their majority cost. Figures 13 illustrates the consequences for a sample of horticultural crops.

Few businesses in 2015 were creating profits as a percentage of turnover above the figures in the right-hand column, and with static (or reducing) sale prices since that time, the continuing viability of a number of crops has relied on improvements in productivity. In some cases, this has been possible – the development of Long Cane raspberry production would be an example – but in others it has not, with production now either marginal or loss-making. The threat to home-grown supply is clear.

The major issue facing the UK grower for 2021, however, is labour supply. As many as 75% of the anticipated annual requirement of around 80,000 seasonal workers are likely to be new recruits who, to date, have come almost exclusively from the EU; this supply will cease completely on 31st December 2020. At the time of writing there is still no

Figure 13 **Seasonal Labour Cost Increases - 2016 to 2020**

Crop	Labour Requirement Hours/Tonne Meridian	Labour Cost 2016-20 Increase £ per Tonne	2016-20 Increase % Illustrative Sale Price
Broccoli	22	58	8
Asparagus	300	780	12
Lettuce	40	104	10
Dessert Apple	30	78	10
Strawberry	140	364	11
Raspberry	350	910	13

Sources: Andersons

decision from the UK Government as to whether it will raise the 10,000 allowance under its Seasonal Agricultural Workers Scheme (SAWS) for non-EU workers.

Any assumption that the shortfall in requirement can be met by UK nationals overlooks the fact that a significant proportion of horticultural production is undertaken in rural areas (e.g. Lincolnshire, Cornwall, eastern Scotland). These are some distance from centres of population, precluding daily travel for UK workers. With existing commitments to accommodation and family, how many can or will be prepared to leave home for temporary employment? The problem for the grower is that each new worker requires a significant investment in initial training and subsequent coaching. Furthermore, new employees need to gain experience before they can operate at a rate that is commercial – which can take up to a full season. In 2020 a number of UK growers found that, having made this initial investment, they lost UK workers when they acquired a permanent position elsewhere.

> ***Without a significant increase in the numbers allowed under SAWS it is inevitable that home-grown production will reduce at a time when it is needed more than ever.***

Without a significant increase in the numbers allowed under SAWS it is inevitable that home-grown production will reduce at a time when it is needed more than ever. Perhaps the approach of policy-makers may change when the media-savvy consumer becomes aware of the consequences for both choice and cost of home-grown fresh produce?

Topical Issue **Vertical Farming**

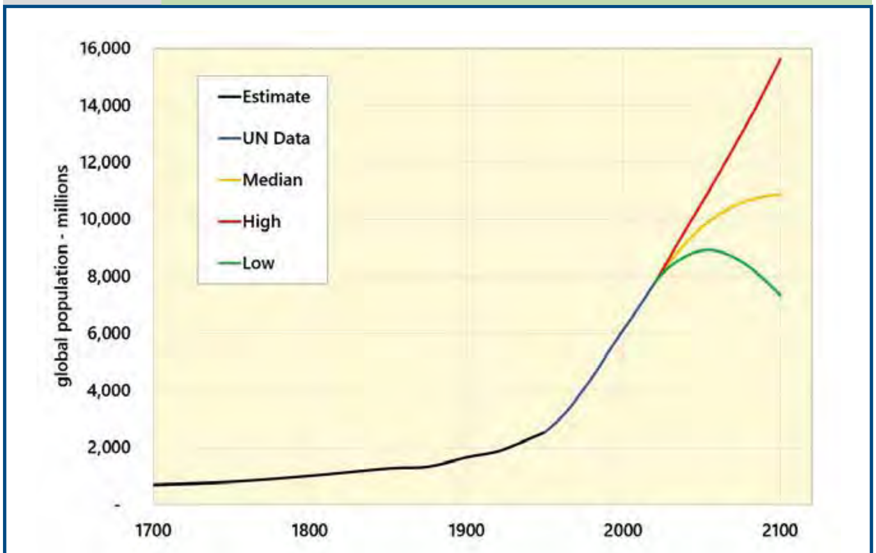
ANNABEL GARDINER

A post-Covid-19 world has evolved; restricted travel has left many people making the most of their home environment and utilising green space. Gardens have been re-landscaped across the country and many have taken to producing their own fruit and veg. The chance to delve into a new hobby, combined with the worry of food scarcity during the pandemic has transformed many urban locations. Not only has the UK seen a rise in domestic urban farming but commercial urban/indoor/vertical farming has also begun to take off. Vertical farming is becoming more and more popular in urban locations. For example, in London, below the streets of Clapham 'LettUs Grow' now produces salad leaves.

More prevalent extremes of weather and climate change will have no effect on indoor farming, promising enhanced food security in the future. Yields should improve due to the removal of external weather patterns and the optimum adjustment of crop growing requirements. One acre of vertical farming is said to offer the same output as 4-6 acres of conventional outdoor capacity. According to some sources, over 10 million hectares of arable land are lost globally each year to development or degradation. In addition, currently 80% of remaining agricultural land worldwide is reported to have moderate or severe erosion. Land is not infinite and our resources must be utilised more sustainably. By 2050 the global population will likely grow by another 2 billion people; indoor farming systems have the capability to deliver food all year round. Yield stability will lead to price stability; a steadier food supply will lead to a reduction in price fluctuations, reducing the risk of investment.

By 2050 the global population will likely grow by another 2 billion people; indoor farming systems have the capability to deliver food all year round.

Figure 14 **World Population – 1700 to 2100**



Source: UN / ANDERSONS

Healthier food has and will continue to be demand driven. With consumer concerns over pesticides, indoor farming, with its ability to control the growing environment should drastically cut the use of artificial pesticides as field pests will no longer be present. Water availability is another issue rising up the agenda. With controlled-environment farming, the opportunities for water recycling will be perpetual; vertical farming uses up to 95% less water than conventional farming. Better use of space in urban locations will reduce food miles; the UK imported £11.5 billion worth of fruits and vegetables in 2019; this was approximately three quarters of total fruit and vegetable consumption in the UK.

Green energy can be utilised; Low Carbon Farming has built two glasshouses (a total of 28 Ha) next to Anglian Water treatment facilities, and are home to the largest heat-pump system project in the UK. Sewage works heat is utilised by the greenhouses and in addition CO_2 enrichment will be provided by an onsite electricity plant. The project expects to grow more than 10% of the nation's tomatoes and provide circa 360 permanent jobs, with an additional 100 during the peak season.

Vertical farming is likely to remain a niche for the foreseeable future limited to high-value, low volume crops.

Breeding programmes for crops to be suited for indoor and vertical conditions will need to be further established in order for this new industry to flourish, John Innes Centre researchers have bred a broccoli variety suited to indoor conditions.

However, the initial investment required for an indoor vertical system is currently immense; Low Carbon Farming's recent build cost £120 million. Other estimates show the total cost for building a 60 hectare vertical farm (the building, lighting, heating, labour etc) is approximately £75.2 million. Once the carbon embedded in the infrastructure is accounted for, the sector's 'green' credentials are somewhat reduced.

Vertical farming relies entirely on technology; a loss of power even for a day could lead to a crash in yield and prove very costly for the grower. For all these reasons, vertical farming is likely to remain a niche for the foreseeable future, limited to high-value, low volume crops – particularly in the salad sector. It seems unlikely the economics will stack-up to produce something such as maincrop potatoes under these systems anytime soon.

Even so, as a niche it could be substantial and will expand. The industry is forecasted to grow by 21% by 2025 and is attracting interest from significant investors. A reliable income stream is (almost) guaranteed, no external factors with the ability to affect yield are present, an increase in price stability and an assured reduction in agriculture chemical spend will leave many leaning towards this new way of food production.

Dairy

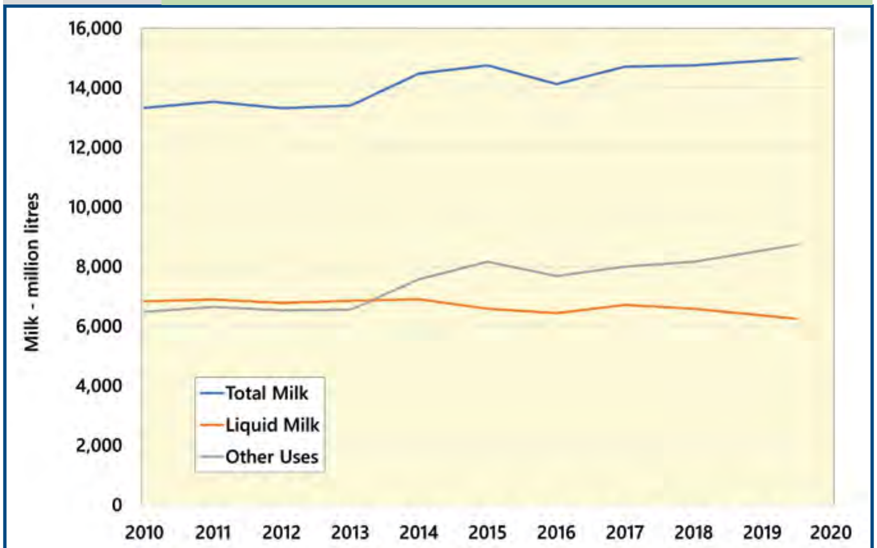
MIKE HOUGHTON,
OLIVER HALL AND
JAKE ARMSTRONG-FROST

For most in the UK dairy sector this has been a relatively stable year in respect of milk prices, with the exception of those badly hit by Covid-19 and the loss of the Food Service market. It was perhaps reassuring just how quickly the dairy food chain did adjust and the positive response from consumers with an increase in doorstep/direct sales milk and a lift in cheese consumption.

At the time of writing the average UK milk price is around 27.6ppl. Disappointingly, this is 10% lower than the average EU farmgate price which is equivalent to 30.15ppl.

There can now be little doubt that the liquid sector, once seen as the premium outlet for milk, has much to answer for in encouraging systems of milk production that are generally much higher cost.

Figure 15 **UK Milk Market – 2010 to 2020**



Source: Defra / Andersons

In the EU just 11% of milk output is for drinking (compared to 48% in the UK) with the rest processed. As the UK continues its shift towards manufacturing with the ongoing decline in the demand for liquid milk, will this lift average prices going forward? Perhaps this is a reflection on the 'stranglehold' UK retailers appear to be able to apply to the sector, ensuring the margins for the farmers and the processors remain wafer thin?

There can now be little doubt that the liquid sector, once seen as the premium outlet for milk, has much to answer for in encouraging systems of milk production that are generally much higher cost. Level supply, longer housing periods, less reliance on grazed grass, and higher cost in terms of labour and power requirements are all legacies of the liquid market.

The focus for the future should be on efficiency and not output. Our most profitable clients are those practising low cost, medium output, grazing-based systems with the yield from forage at >4,000 litres. Other key characteristics include block calving, cross breeding to enhance milk solids, and an absolute focus on cost control.

UK dairy farmers will face additional challenges over the next few years with the end of the Brexit Transition Period at the start of 2021, the demise of the BPS by 2027 and legislation to cover slurry pits by 2026.

Most reports suggest Brexit should not be too bad for the dairy sector given the UK is not self-sufficient, and our standards are some of the highest in the world. Exporters may not target the UK aggressively, given other growing markets around the world (i.e. China). The Chinese Government is encouraging its population to consume 300g of dairy a day which could take up most of the world's 'surplus' milk.

For most, the BPS equates to 1-2ppl and so will be sorely missed – considering Stewardship/ELM should be a priority for all producers.

Emissions could be the industry's greatest challenge, with covering slurry pits just the tip of the iceberg.

Emissions could be the industry's greatest challenge with covering slurry pits just the tip of the iceberg. On a global scale, AHDB reported that if all cows performed to the same level of output as the average UK cow (7,900 lts) the population of dairy cows in the world would fall from 265 million to just 83 million!

The industry needs to lead this debate and not be driven by it. Dairy farms already sequest lots of carbon and can do more; diets could change to exclude imported items such as soya (M&S and Waitrose are leading this initiative); slurry can be used more efficiently to save fertiliser (and NVZ restrictions need more science to match crop growing conditions); more clover rich swards can be grown; genetics need to focus on low emission cows and most dairy farmers could make more of renewables to run electric vehicles – at least around the yards.

There will be much to think about for those committed to a long-term future in the industry with the key areas to focus on being quality not quantity, and efficiency not output.

Beef

CHARLOTTE DUNN AND BEN BURTON

The second half of 2020 has proved how finely balanced agricultural commodity markets can be. In early May, the GB average cattle price was as low as 325p per kg deadweight, by mid-August it had reached 375p per kg deadweight, a 15% increase; this brought much-needed relief to a sector where the majority find it hard to make profits.

A tightening of domestic supplies, reduced imports and strong retail demand were the main factors. The latter was driven by a rise in mince consumption over lockdown and favourable spring weather facilitating barbeque demand which offset the decline in the eating-out market.

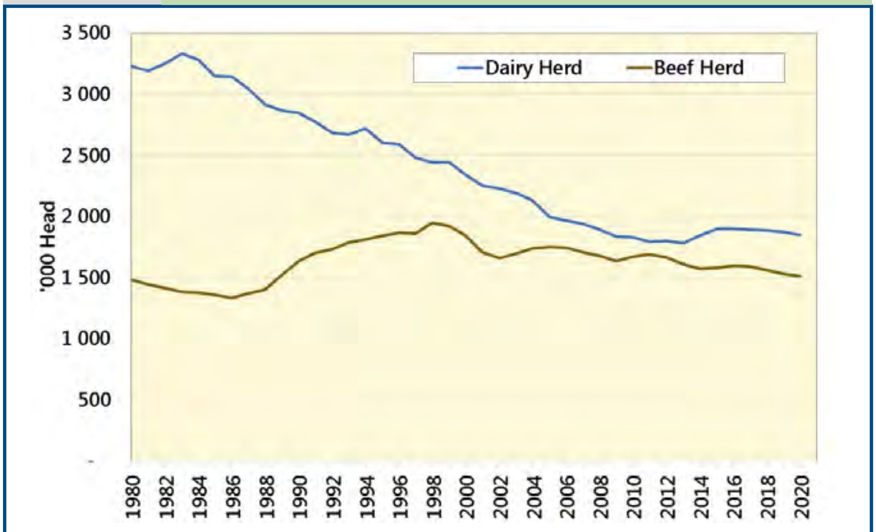
The size of the UK beef industry continues to contract. Latest data from the June Census shows both the UK suckler and dairy herds contracting by around 1% compared to a year earlier.

We expect this trend to continue for both dairy and beef cows. The average yield in the UK dairy herd is likely to continue to increase, meaning fewer cows are needed to produce the same volume. With regards to suckler cows, the continued lack of profitability and reducing support payments on which the majority depend are likely to be the main factors driving down numbers.

The effects of reducing herd sizes on UK beef production may be offset to some degree in future by the increasing use of sexed semen in the dairy herd. Sales of sexed dairy semen accounted for just over half of dairy inseminations in the year to March 2020, up from 32% the year before. Looking at the proportion of beef semen used in the dairy herd this has increased from around 25% in 2013 to 48% today. Very simply, with fewer cows needed to provide replacement dairy heifers, more cows can be served with beef semen providing more beef calves. These dairy-cross beef calves are likely to make up a larger percentage of UK beef output in the future, assuming

> *Dairy-cross beef calves are likely to make up a larger percentage of UK beef output in future, assuming they can be finished at a profit.*

Figure 16 **UK Herd Sizes – 1980 to 2020**



Source: Defra / Andersons

they can be finished at a profit.

In the short-term supplies of UK prime cattle look set to remain tight. British Cattle Movement Service data at 1st July 2020 reported cattle 12-30 months of age, those most likely to be slaughtered in the next few months, down by 76,500 head (-4%) on the year. Looking further ahead, the number of animals available for beef production under 12 months of age was similar to the previous year. The number of beef cross animals was up and pure dairy males down, reflecting the trend in use of sexed semen outlined above.

The UK imports a lot of beef, most notably from Ireland, and reduced imports, down 11% for the first 7 months of 2020, was an important factor in the price increase seen. In the short-term Irish data suggests supplies will remain tight but looking further ahead there is an increased number of calves on farm in Ireland as Covid-19 has limited live calf export opportunities. Supplies may well increase in 12 to 18 months time.

Whilst the exposure of the sheep industry to trade disruption and tariffs following the UK leaving the EU Single Market at the end of the year is well trailed, the beef sector is far from immune. By volume, the UK exports around 20% of beef produced and imports around 35% of that consumed. Whilst simply replacing imports with home production may sound very appealing the situation is more complex, not least as the export trade helps to maximise the value of UK production - often exporting unwanted cuts and offal.

However, in its simplest form, with imports much larger than exports, a No Deal Brexit could increase beef prices, at least in the short term. In the longer term, if the UK strikes trade deals with the wider world, any increased access given to low-cost producers in the big exporting nations such as the US, Brazil, Argentina and Australia could reduce them.

Looking to the future, whatever happens with Brexit a permanent shift in beef prices to levels significantly above the current long-term average of around 355p per kg deadweight would seem unlikely. Hopefully sufficient protection will remain to prevent the industry being undercut by lower cost imports whose standards of production may be below our own.

The true costs of production for many suckler beef producers, to include a return on their own labour, is between 380 and 410p per kg deadweight. If the beef price remains in its current range, a continued decline in suckler cow numbers is likely.

“Whilst simply replacing imports with home production may sound very appealing the situation is more complex, not least as the export trade helps to maximise the value of UK production - often exporting unwanted cuts and offal.”

We continue to see a huge range in the performance of suckler beef enterprises; feed, forage, labour and machinery costs are the biggest variables and those with the very lowest production costs have typically found innovative solutions for taking costs out of these systems. In the short-term, increases in straw and concentrate feed prices are increasing the costs of production for many in the sector.

If beef cross and dairy bull calves are to help offset any fall in production from the suckler herd ultimately it will depend on whether these calves can be finished at a profit.

Some integrated supply chain models are beginning to evolve in the dairy beef sector. It would be wrong, however, to think these models can produce beef at a much lower price. On a cost of production basis, retailers are likely to have to pay a premium for the product over and above the current long-term market average. The extent they are willing to do so may depend on such things as:

- *The value placed on a fully traceable, regular supply of what can be a very uniform product*
- *The quality of the product and ability to market it as such*
- *The value consumers may place on the full traceability such systems can offer*
- *Their responsibility to help with acceptable practice with regards to surplus calves from the dairy herd.*

It would be good to see similar initiatives begin to develop in suckler beef production.

Sheep

DAVID SIDDLE

Having now contributed to the sheep article in Outlook for more than 20 years, trying to summarise the prospects for the year ahead and beyond for this sector of the industry has never been more difficult.

In this year's article we have commented as usual on sheep numbers, trends and likely levels of production as well as reflecting on the key fundamentals which underpin the current structure of the UK sheep industry. Rather than attempting to forecast the potential effects for unknown Brexit outcomes and the economic consequences of Covid-19, we have looked at what commercial businesses might learn from some of the study work Andersons has carried out for AHDB and Meat Promotion Wales which looked to identify the key characteristics of high performing beef and sheep farms.

Where Are We Now?

The breeding flock in December 2019 at 13.8 million head was little changed year-on-year but smaller than it has been in recent times.

Looking forward, some continued contraction in the breeding flock seems the most likely outcome with Brexit uncertainties in the short term and changes to farm support payments longer term being the main drivers. Low levels of profitability excluding support payments for many and an aging work force of family labour on which much of the sector depends, are likely to continue to put pressure on flock numbers.

The 2020 lamb crop is forecast to be marginally smaller than 2019 at 16.8 million head, with weather at lambing good for most albeit ewes did experience a wet winter. Sheep meat production in the 2020 calendar year is forecast to decline by 7% with the lamb kill down 4% and the ewe kill down 9%.

> *Trying to summarise the prospects for the year ahead and beyond for this sector of the industry has never been more difficult.*

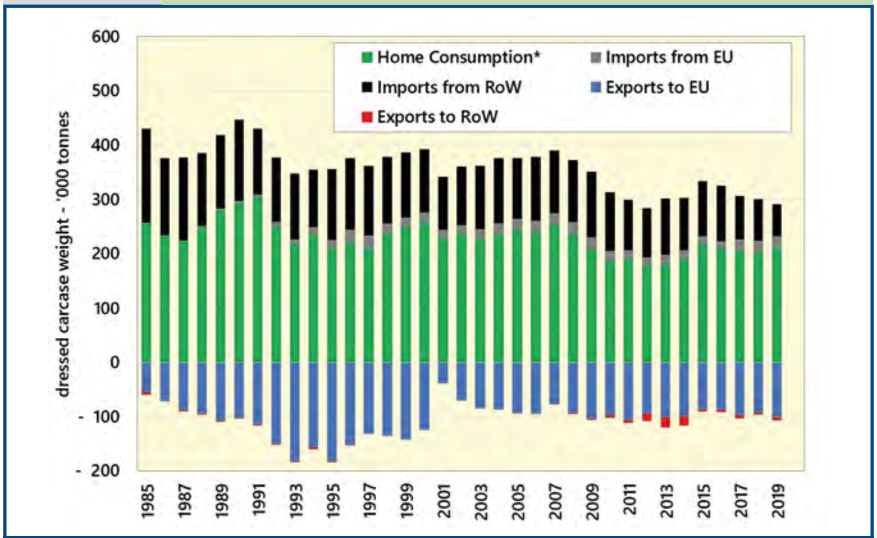
Lamb is a relatively expensive and premium meat choice for most consumers, often eaten out of the home. The immediate impacts of Covid-19 in terms of the closure of restaurants and perhaps longer term in terms of personal finances, suggests consumption levels are likely to continue to decline. As Figure 17 shows, the consumption of sheepmeat has been in decline in the UK for many years (the total height of the columns is the amount consumed each year in the UK).

Whilst domestic production is currently very similar to consumption, international trade is a very significant factor for the industry. The seasonal nature of UK production creates a sizeable surplus in late summer and autumn and a deficit in spring and early summer. This surplus has formed the basis of a very successful export trade with an average of 35% of the total UK lamb crop being exported over the last decade. 95% of exports are to the EU, half of which go to France. Frictionless access to these markets remains paramount if the industry is to continue at its current size and with its current structure.

New Zealand dominates imports largely as a legacy going back to Commonwealth days. Recent sheep meat prices have been underpinned by reduced levels of imports from New Zealand, both to the UK and the EU, with supplies tight following drought. Strong demand from China which has a shortage of meat as a result of African Swine Fever decimating its pig herd has also diverted New Zealand sheep meat exports from both UK and EU markets with this looking set to continue into 2021.

Brexit permitting, there remains a great opportunity to continue to build on the successful export trade we have built up over many years. In addition, the sector must look to deliver a high quality, consistent, premium product to the UK retail sector which is, at least for the present time, looking for a home-produced product. However, even with a positive Brexit outcome, with a Free Trade Deal, we would expect both production and consumption to continue to trend downwards.

Figure 17 **UK Sheepmeat Market – 1985 to 2019**



*Source: Defra / ANDERSONS * domestically produced lamb consumed in the UK*

What the Best Do

The various studies we have carried out which have looked to identify the key characteristics of high performing beef and sheep farms. These found very similar trends, with the three most influential factors contributing to the differences in financial performance being;

- *Minimising overhead costs*
- *Understanding the market*
- *Focusing on relevant detail*

Higher performing farms all had lower overheads than the rest. No farmer can operate in the top performing quartile without a keen focus on cost control. When producing a commodity product, low cost production is essential.

Overhead Costs: Labour is a key element of overhead costs. The requirement for labour on sheep farms varies throughout the year, with lambing being the peak labour period. Top performers keep lambing short and concise, prolonging lambing will require more casual labour and ultimately lead to varied growth rates which will potentially complicate management practices for the rest of the year.

Many top performing farms have developed systems and focussed on breeding and selection which reduces labour input at lambing such as being able to lamb unassisted and mothering ability. Breeding can also reduce other time-consuming traits, the principle one being lameness.

Power and machinery is another big contributor to overhead costs. Efficient sheep farms can operate with very little machinery. Contractors can be used to reduce costs in many situations. Once a machine has been bought by

Figure 18 **Sheep Costings - 2017**

£ per ewe	Lowland Ewes			Upland Ewes			Hill Ewes		
	Bottom Third	*Ave.*	*Top Third*	*Bottom Third*	*Ave.*	*Top Third*	*Bottom Third*	*Ave.*	*Top Third*
Net Output	90.25	101.12	111.14	77.63	94.22	120.43	65.32	85.81	120.11
Variable Costs	62.22	51.65	40.91	48.69	44.31	42.42	41.42	43.00	42.39
Gross Margin	28.03	49.47	70.53	28.94	49.91	78.00	23.80	42.81	77.71
Overheads	66.31	41.97	25.24	42.15	32.92	28.37	45.83	34.38	26.54
Rent & Finance	14.65	12.00	8.32	15.42	10.54	7.32	12.89	9.87	9.24
Profit / Loss	-52.93	-4.49	36.97	-28.63	6.45	42.31	-34.92	-1.43	41.93
Variation	+/- £89.90 per ewe			+/- £70.94 per ewe			+/- £76.85 per ewe		

Sources: HCC Data analysed by Andersons

a business, its cost remains with the farm for several years; hence purchases should be carefully appraised. The capital cost of a purchase is often the major or only thing focussed on but over its life on the farm, fuel, repairs, insurance as well as the costs of an operator need to be taken into account.

Housing and the production of (expensive) conserved winter forage can add to both labour and machinery costs. Many of the best performing businesses have looked at these costs very closely and developed innovative solutions to significantly reducing them.

Figure 18 summarises the results from the Welsh Red Meat Benchmarking Study carried out by The Andersons Centre, it shows a huge variation in performance.

"No farmer can operate in the top performing quartile without a keen focus on cost control."

Whilst output is clearly crucial, the other dominant factor is the lower level of overhead costs of the best performing businesses.

Understanding the Market: The best businesses understand what the market requires and deliver it. They are not hung up on breeds or non-commercial traits. They are able to deliver a consistent product which may not 'top the market', but one which is sought after, can be produced from a low-cost base, and hence give the best chance of selling for a profit.

Focus on Detail: If you want to improve something, you need to measure it, analyse it, benchmark it, research it again and then change something to improve it. This is where KPIs (Key Performance Indicators) and benchmarking can be very beneficial. Some examples of sheep flock KPIs include:

- *Lambs reared per 100 ewes put to the ram*
- *% of lamb losses from scanning to finishing*
- *Average daily liveweight gain (DLWG)*
- *Quality of carcass*
- *% lameness*
- *% of flock requiring lambing assistance*

In summary, it has been widely proven that the factors mentioned above (reducing overhead costs, understanding the market and measuring performance) will regularly place farmers into the top quartile of performance when exercised effectively. Being able to adapt and change the way farming practices have traditionally been carried out is now, more than ever, crucial for success.

Pigs

HARRY BATT

Will the disease sagas roll on into 2021? 2020 has seen trade disruptions due to African Swine Fever (ASF) and Covid-19 altering the landscape of the global pig industry, almost on a weekly basis.

At the time of writing, Germany's trade with Asia seems to have been halted due to the latest ASF outbreak. This means German exports will enter the global carousel looking for a new destination. Asia could find sourcing pork harder as time goes on, with Brazilian supply likely to be curtailed by the Covid-19 outbreak. The evidence to date suggests that the pandemic has limited labour availability within supply chains which has resulted in backlogs in processing plants. This in turn has led to price rises for pigmeat.

In the UK, the pig industry has had a positive year with an uplift in prices for producers (albeit drip-fed for some B&B contracts). The sector has made further improvements in self-sufficiency with 7% growth in just two years, to 59.4% (2019). This trend could continue over the next few years with supplies around the world remaining tight due to ASF and Covid-19. Despite some forecasts that the breeding herd would increase due to better prices,

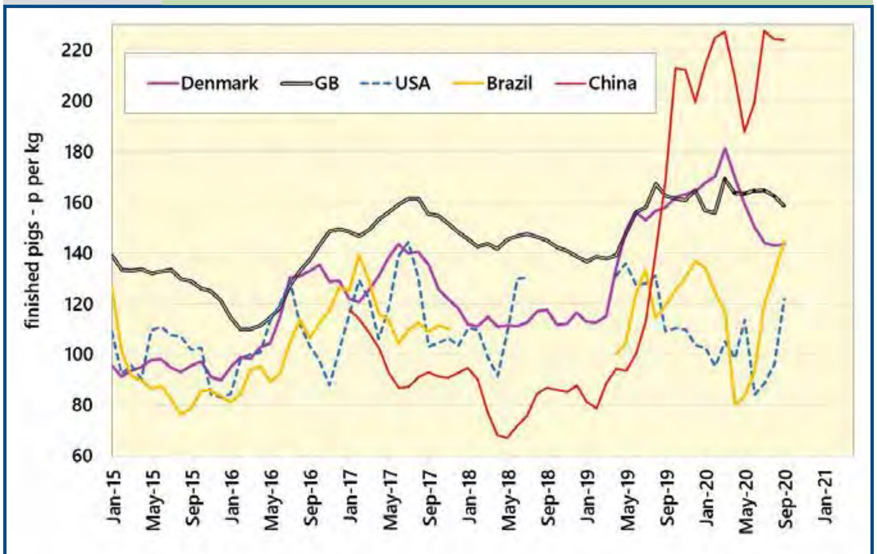
> ***The pig industry has had a positive year with an uplift in prices for producers.***

the most recent Defra June Survey figures showed a contraction with the herd at its lowest number since 1983. Instead, the rise in pigmeat output is being driven by more piglets per sow and higher finishing weights.

We must remember that the UK is a small producer. The UK has approximately 7 pigs to every 100 people, whereas in Denmark, Netherlands and Spain this is 215, 70 and 63 pigs respectively. In Denmark, the average breeding herd size is >1,800, compared to 680 sows & gilts in the UK. Furthermore, these will usually be on an indoor production system, which is the system of choice for European countries.

As an industry, should we be

Figure 19 **Global Pig Prices – 2015 to 2020**



Source: Bord Bia /Andersons

trying to compete head-on with these other countries? We operate on a different playing field to our European counterparts, let alone pig producers in North and South America. This is due to the UK's challenge from planning/building regulations, higher health and welfare standards and the cost of inputs.

Therefore, we should look objectively, like any other non-agricultural industry would, at the benefits and the Unique Selling Points (USP) of our UK sector. Why not use Brexit as an opportunity to develop a market based on features unique to the UK sector? We are being told that consumers are eating less meat, and are leaning towards quality not quantity. There seems scope to follow the poultry model and focus on offering 'free-range' and high welfare pork, rather than the UK product being 'lost' in the commodity pork which the rest of the world produce. Commodities tend to decrease in real terms value each year; marketing more UK pork as free range/outdoors will create a point of difference and should prevent such value deterioration.

There seems scope to follow the poultry model and focus on offering 'free-range' and high welfare pork.

To achieve this the focus should be on creating a three-point plan.

1. Public Perception: 40% of UK breeding herds are in outdoor production systems - a truly unique point of difference for global pork production systems. The egg industry has already undertaken the marketing for free-range, with the perceived benefits appealing to a wide-range of consumer group. The pork industry could adopt a new strategy with a bespoke British Produced Free-Range label. This should be widely advertised and marketed via mainstream media sources.

2. Health & Welfare: At the time of writing this article it is unknown whether the 2020 RUMA target (99 mg/kg) has been achieved. This is higher than both the Danish and German average antibiotic usage (in 2017) of 39.4 mg/kg and 89 mg/kg respectively. The UK's challenge is to get closer to the World's top performers, whilst operating a different system and coping with the impending Zinc Oxide Ban in 2022. Despite this, our industry's welfare standards are some of (if not) the best in the world and this should be well publicised.

3. Resource Management: Given the recent increasing scrutiny on environmental management and 'Net Zero', our industry should embrace the opportunity to evolve to achieve the NFU's target of a Net Carbon Zero agricultural industry by 2040. Can the sector look to profit from a changing arable rotation working collaboratively with other farms and increasing ELM opportunities?

Poultry

LILY HISCOCK
AND ED CALCOTT

With free range egg prices moving from a depressed position at less than 70 pence per dozen last year to prices in the marketplace today of over 90 pence per dozen and strong demand from homeworking consumers aiming for the British Bake Off series 2021…, what a difference 12 months makes!

The 'cage free' commitment made by the retailers by 2025 (and earlier for some) looms ever larger and there are big concerns in the egg sector that perhaps they have bitten off more than they can chew. Free range currently represents 52% of total egg packing station throughput as shown in Figure 20 below. Within the retail sector the share is much higher at 68%.

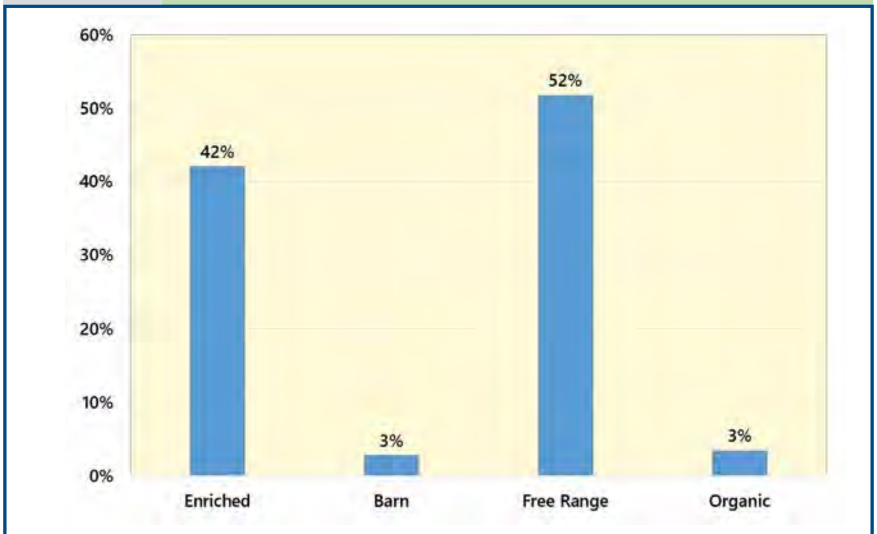
If consumption remains unchanged, to increase total free-range production to 65% from the current 52% by 2025 would require more than 4 million extra free range birds. Put another way, this is more than 250 extra 16,000 bird free range egg units. To achieve this by 1st January 2025, would require more than one new unit to come online every single week. With Planning Permission for new sites remaining challenging and Avian Influenza (AI) discouraging single site growth, this target looks nigh-on impossible.

With no more enriched colony eggs from 2025, where does the 'value-egg' offering on shop shelves come from?

In the short term, this is likely to result in strong demand for existing producers and prices will reflect this. Brexit will only exacerbate the tight market, with potentially reduced import opportunities, particularly for liquid egg. Perhaps a few golden years that free range producers should look to capitalise on, ready for more difficult times to come?

With no more enriched colony eggs from 2025, where does the 'value-egg' offering on shop shelves come from? Some retailers are looking to barn eggs for this (just 3% of the existing marketplace), by converting existing colony sheds. However, most enriched

Figure 20 **UK Egg Packing Station Throughput – 1st Half 2020**



Source: Defra

colony producers are still paying off investment from 2012 and, with barns requiring a lower stocking density (30%-40% reduction in birds), the new investment does not look appetising or economically viable at over £18 per bird to convert these sheds.

The cost of production is somewhere in the region of 5–10 pence per dozen less for barn than free range (compared to 20+p per doz for enriched colony). Perhaps not exactly the value offering the retailers were after?

In our opinion, barn will see some growth, perhaps up to 10% of the market by 2025 but in most cases, free-range may become the 'commodity' egg offering. The concern is that commodities tend to decline in value over time and this downward pressure will almost certainly be passed down to producers to erode their margins. A two-tier free-range egg market looks likely – 'standard' free range and the 'differentiated' offering.

This perhaps is where the opportunity lies for free range egg producers – tapping into the growing culture for high welfare, environmental credentials, foodie culture and home cooking. The egg is a versatile, healthy offering which meets many of the demands of the younger 'Gen Z'.

In the short term, free range egg producers should look to:

- *Obtain contracts with stable pricing across the board (XL to Seconds), rather than going for the highest paying packer today!*
- *Develop a good relationship with your packer and meet their requirements i.e. work together to develop 'new' eggs and timing peak lay to meet demands*
- *Focus on efficiency and high quality – fast turnaround times, reduced antibiotic usage, clean eggs with minimal seconds.*

In the longer term, producers should review where they wish to be post 2025. What are your objectives – to be a highly efficient producer, operating at scale and focusing on output or a more modest scale, targeting the premium / local market with the focus on welfare, eating quality, nutrition, environment etc. A 'price taker' or 'price setter'?

Turning to the meat sector, 2020 has been a testing year. Covid-19 has had an impact right through the poultry supply chain; from difficulties in securing wood shavings for bedding; acquiring PPE/dusk masks for farm staff; and the unfortunate closure of some processing factories due to clustered outbreaks of the virus. The latter has led to factories working together with extra shifts to take in additional birds to minimise the numbers which sadly had to be culled on farm. These shutdowns are costly and have a detriment on bird welfare and margins. There is current lobbying to allow factories to operate on a skeleton crew, rather than shutting down for two weeks to allow staff to isolate which will reduce the possibility of on-farm culling.

> ***The need to shout about the quality of British chicken to the country's population has never been higher.***

Further mitigation may lead to reduced placings across farms by 10% to create spare processing capacity so companies can divert birds elsewhere should shutdown be necessary. This makes factory communication nearing clear-out time even more so important; turnaround periods may be reduced so ensuring good communication with sub-contractors for cleaning and bedding is vital. Insurance should be checked to make sure there is cover should your factory close and there are no alternatives for the birds; disposal for on-site culled birds is in the region of £100 per kg.

Meanwhile, higher welfare categories of free range and organic chicken, although relatively niche, are experiencing firm demand. During lockdown, people looked for quality and were more interested in the origins of their food. Butchers shops and farm shops have done and should continue to do well with these ranges.

As we near Christmas there are several concerns surrounding turkey size and seasonal migrant labour for processing work. Currently EU workers will have to quarantine for two weeks prior to work; then may have to do so when they return to their home-country. This adds another month onto their already short holiday time. There must be efforts to try and recruit UK labour for the roles to try and reduce the cost of paying migrant staff to isolate.

Turkey producers worry about the 'rule of six' carrying on into Christmas and that sales of large turkeys will be difficult. As the poults are ordered in the Spring there is very little that can be done at this stage without forward clarity on Government guidelines. Diets can be manipulated to include less protein and more wheat but there is a risk the unique selling point of eating quality may deteriorate. Alternatively, turkey producers need to start spreading the word about leftover recipes to try and use up the extra weight to avoid giving it away. However, we must also remember that there is estimated to be 4.6

million more people in the country for Christmas due to not being able to travel – these may be of the more affluent proportion of the population. Good marketing is key (not just advertising); small producers really need to tell the story behind their turkeys to give their product identity, something larger retailers cannot do.

Finally, this would not be a poultry piece without mentioning chlorinated chicken, or should it be peracetic acid chicken, which is now more commonly used in US poultry plants? Are US imports a threat to our industry? Both the UK and the US consumers prefer the white breast meat rather than the lower value cuts of wings, legs, and thighs, which both countries export. So, will the American processors flood the UK with chicken given the opportunity? It seems unlikely to arrive in huge volumes due to the combined commitment of several large UK retailers to not sell chicken unless it is produced to UK standards. The need to shout about the quality of British chicken to the country's population has never been higher.

Topical Issue **Carbon and Net Zero**

MIKE HOUGHTON,
HARRY BATT AND
LILY HISCOCK

On the 29th June 2019, Parliament passed the Climate Change Act 2008 (2050 Target Amendment) which has set into law a target to reduce the UK's net emissions of greenhouse gases (GHG) by 100%, relative to 1990 levels. By meeting this legislation, the UK would become a 'net zero' emitter.

The UK agricultural industry is the fourth biggest GHG contributor, which is why the NFU have committed to achieving Net Zero by 2040. To achieve this the challenge is twofold:

- *Alter and adapt farming practices to reduce emissions*
- *Improve and develop carbon sinks to offset the remaining emissions.*

Figure 21 shows the trends in UK agriculture's emissions of the key GHGs and how we might get to net zero.

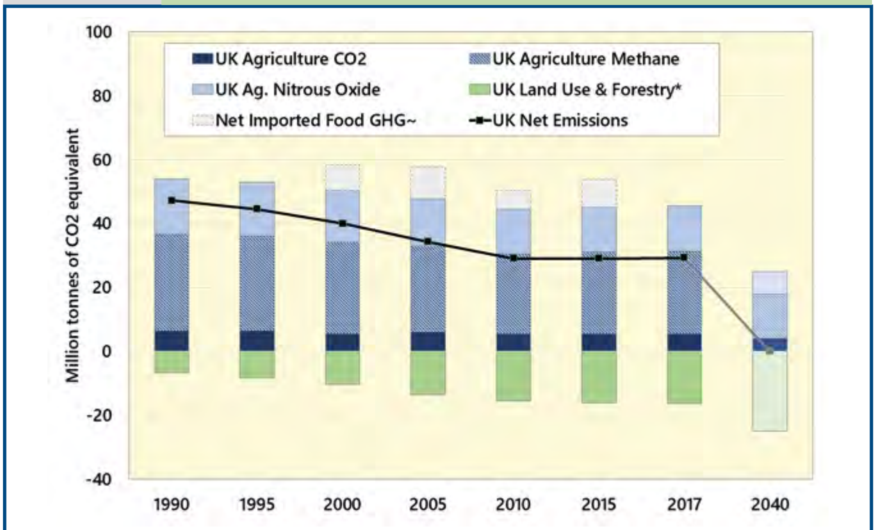
As we set out in Outlook 2020, it is inescapable that livestock are contributors to UK greenhouse gas (GHG) emissions; responsible for 5% of total carbon and 88% of ammonia emissions. On the current trajectory, the livestock sector and farming more generally will not achieve the overarching Net Zero target. Therefore, there is a need for greater innovation and improved collaboration and communication on an industry level if the Net Zero target is to be achieved by 2040.

Whilst this is a challenge it can also be seen as an opportunity. The Committee on Climate Change (CCC) estimates that change in land use policy sufficient to achieve net zero could be achieved through funding of £1.4bn per year – much of which would flow to land managers.

The aim of adopting improved carbon friendly practices should not be to increase reliance on food imports, letting carbon in through the backdoor, but to increase the productivity of UK farms. So how can current farming practices be adapted to be more carbon friendly? Do we currently use land to its optimum potential?

In respect of improving carbon practices, there is a growing requirement for farms to understand their carbon footprint (Step 1). Traction to date has largely been led by processors and retailers, however as an industry we must learn more about what we are emitting. Industry leaders have stated that they expect environment emissions scoring to be commonplace on food

Figure 21 **UK Agriculture GHG Emissions – 1990 to 2040**



Source: DECC / Andersons ** excludes land use related to 'settlements'* packaging within the next two years. Therefore, let's take advantage and be in the best position to tackle the competition. Carbon footprint tools are available at a farm/product level.

Once current emissions are being accurately measured, Step 2 will be to evolve and monitor. Industry must alter land use policy, with land used for food production or the environment (i.e. renewable energy). Farming for food will need to be smarter with practices adapted to be more sustainable. Some examples of this are given below;

- *Gene editing and genomics to produce carbon friendly livestock and plants. The Nobel Prize was awarded to a CRISPR gene editing method which can alter the DNA of animals and plants to improve reduced methane emissions in cattle and rice paddies (if allowed within the UK).*
- *Use of alternative feeds, i.e. 3NOP & seaweed, to inhibit gas release has reduced emissions by up to 30% in trials. These feeds could be a necessity in livestock rations in the coming years.*
- *Utilisation of smart technology - virtual-fencing systems, enabled through a GPS collar, are used in Australia to provide grazing platform flexibility.*
- *Maximise the potential of slurry - Arla have unveiled a biofuel trial generating fuel from slurry (to power their milk tankers), whilst still providing a digestate or solid matter fertiliser for farmers. In addition, there are membrane filtration systems that separate slurry into clean water and a concentrate fertiliser.*

A proportion of current farmland is likely to move into 'carbon-reduction' uses. The CCC estimates this at 20-25% of the land area – a proportion of this land will cease food production entirely, whilst on

> ***There is a need for greater innovation and improved collaboration and communication on an industry level if the Net Zero target is to be achieved by 2040.***

others, some 'farming' will continue alongside the carbon mitigation activities.

Renewable energy production will continue to grow as a land use. A key aim for the Government appears to be the development and utilisation of BECCS (Bioenergy with carbon capture and storage). This will involve more growing of feedstock for energy production, with biogas plants then utilising technology to store carbon underground, making the energy production a Net Zero process.

It seems clear that part of the drive towards net zero will involve more tree-planting - as set out in the Contributed article in this year's Outlook. But there are also opportunities at smaller scales. It is estimated that enhancing the existing hedgerows in the UK could increase CO2 storage by up to 500,000 tonnes each year. There are many other land uses that can sequest significant carbon – especially peatland, but even such 'ordinary' land as permanent pasture. The key issue for many farm businesses is how the provision of carbon reduction is going to be measured and monetised. In England, the ELM scheme may provide public funds. A comprehensive economy-wide carbon trading scheme would provide a more liquid and robust alternative. Over the next decade the provision of 'carbon services' may become an important income stream on many farms.

Scotland

ALEX CARAFFI AND
BEN KELLAGHER

Scotland arguably started 2020 in a significantly better state than much of the rest of the UK, with the majority of the planned winter crop in the ground and growing well. In fact, in the North East of Scotland the crops at the turn of the year were looking as well as your writers have seen in the last decade. Subsequently, the dry spring and early summer led to yield penalties on many winter barley crops whilst other crops received rain in time so as to not cause too many challenges. Harvest got an early start and motored through the later part of July and into August before a break in the weather gave a few people headaches with ready crops which could not be cut. Harvest was mostly completed in good time with yields performing well.

The impact of Covid has been seen in the fall in demand for malting barley and consequent weakness in spot prices, meaning that for the second year in a row this was at a discount to wheat by £20-£30 per tonne. There was also difficulty in meeting the quality spec as harvest wore on. How the 2021 season pans out will be interesting and those growing malting barley are well advised to make sure they are maximising the price they can achieve from the available forward contracts.

> *Businesses should not miss the opportunity to consider how they may fare when support schemes definitely change in 2025.*

The dry spring had significant positive impacts on the livestock sector, with lambing proceeding with as much ease as in any of the best years. Those flocks lambing a bit later were slightly hampered by the dry weather and slower grass growth. We all know what has happened with breeding sheep values but perhaps one of the biggest stories has been the high available price for light lambs. We have seen many producers taking advantage of these prices to clear the decks early and give themselves a gentler autumn and winter. It will be fascinating to see whether those taking the gamble with these expensive stores can make them pay in 2021. The beef sector has been on a rollercoaster, with the floor falling out of the market during the start of the global pandemic and then recent recoveries in finished and store prices buoying producers of late.

The global pandemic has clearly had an impact on the wider economy. Aside from the impact on the malting barley and beef sectors already mentioned, there is likely to be long term impact on demand for many of the premium commodities produced on Scottish farms. If we fold in the recent import tax on Scottish whiskey into the USA we might be advised to think carefully about future crop rotations including large spring barley areas.

The Scottish Government has again pulled the rabbit out of the hat with the payment of the BPS loan scheme worth 95% in September 2020. Where they will go in future years with payment periods is difficult to know. However, it seems unlikely to be a popular decision to go back to payments in December as this would mean a substantial gap between payments in one year. The convergence monies paid in 2020 provided a huge boost to a number of upland and hill businesses and given the full convergence pot has yet to be used we wait to see whether a similar payment is made in 2021.

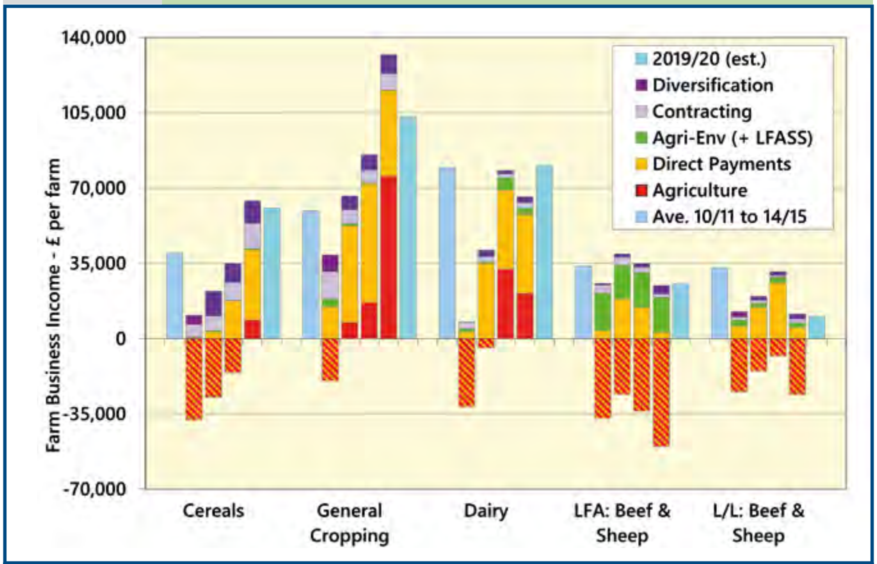
Scotland's Agriculture Bill passed through Holyrood in Autumn 2020. Whilst much of the content was already known, the main additional element was the sunset clause bringing the current schemes to a close in 2024, with a transition period, where new approaches are piloted, from 2021 to 2024. Secondary legislation is now required to bring forward pilot schemes and the continuation of the BPS and LFASS schemes for 2021. This is good news for Scotland's agricultural sector, during a period of much uncertainty, whether it be Covid, Brexit and future trade deals. The sector knows one of its' key sources of income is here to stay for the next few years. Figure 22 highlights just how much of the profit on Scottish farms is derived from the BPS and, in the hills, LFASS.

Businesses should not miss the opportunity to consider how they may fare when support schemes definitely change in 2025. Those businesses that refuse to consider the future now may miss a period where they could consolidate profits, or make investments in their business which will make them stronger.

The next Scottish Parliamentary elections will be upon us in May 2021 and perhaps this may inform some of the payments of convergence monies in the early spring. It is difficult to suggest at this time that there will be a meaningful move away from the SNP being in control of Holyrood. They have shown strong support towards the rural vote in recent months, but whether they are able to maintain support throughout a new Parliament remains to be seen. Will agriculture be top of the list while the economy recovers from a pandemic, establishes itself with new international trading conditions, and braces for a period of discussion surrounding a referendum on Scotland's independence? It seems unlikely to be a high priority and it is doubtful that the sector will get increased levels of support. The best outcome might be that the industry is allowed to continue on in much the same way it does at the current time.

Scotland's rural businesses continue to prove that amongst them are some fantastic advocates for agriculture, some excellent entrepreneurs, and brilliant business operators. We hope to speak to many of you in the months to come and wish you all the best for 2021.

Figure 22 **Scottish Farm Business Income (Profit) – 2010 to 2020**



Source: Scottish Government / Andersons

Wales

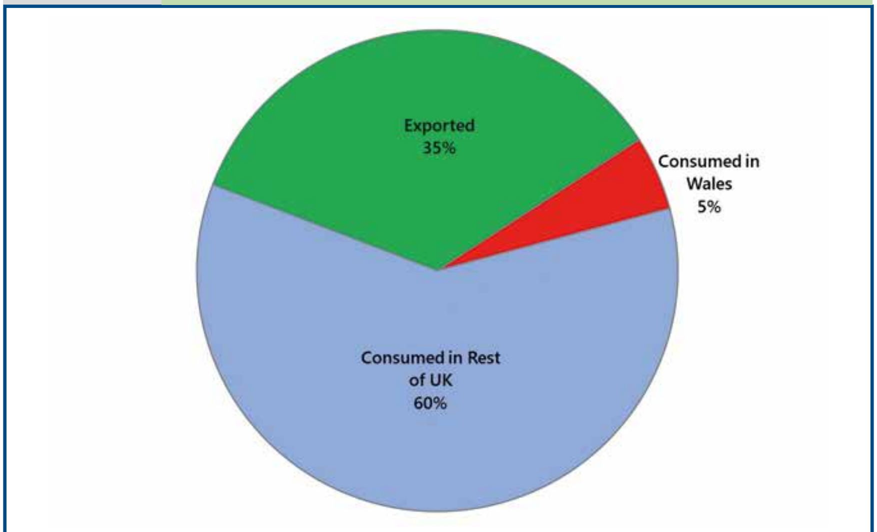
KERRY JERMAN AND DAVID THOMAS

Remarkably, in Wales there currently seems to be an air of calm across the agriculture industry. With above-average output prices across the various sectors and records being broken in Autumn breeding ewe sales for another year, you could be forgiven for forgetting that Brexit is looming around the corner. The effects of Covid-19 has pushed the Principality together, like the other home nations, with local demand for dairy and red meat products increasing, particularly during lockdown. This has given the more entrepreneurial farmers an opportunity for direct sales to

With records being broken in Autumn breeding ewe sales for another year, you could be forgiven for forgetting that Brexit is looming around the corner.

customers and Hybu Cig Cymru, Meat Promotion Wales to push 'local' Welsh beef and lamb - increasing the popularity of village and town butchers. However, this is still a relatively small amount of sales compared to the export market, for lamb in particular.

Figure 23 **Destination of Welsh Lamb**



Source: HCC / Andersons

There is a degree of (false?) security throughout the farming population due to the extension of BPS in the 2021 year which could well be extended into the 2022 and 2023 years. There is still, to date, very little detail on the replacement scheme released, with the general consensus favouring a long transition period for at least 5 years. However, much depends on the size of the pot afforded to Wales once the funding from the European Union dries up.

Without a crystal ball, it is difficult to accurately measure whether the incoming Brexit storm will be no more than a tempest in a teacup or a cataclysmic event. However, there are currently many opportunities for famers in Wales to 'fix the roof whilst the sun is shining' using funds in the extended Rural Development Programme.

Farming Connect will now run to August 2022; continuing to offer funding of up to 80% for one-to-one strategic business and technical advice, training courses to improve Personal Development and also as a stepping stone, joining young farmers with farmers ready to step back in Joint Venture schemes through their Venture Programme. Using this funding to assess your current business' performance is a great starting point for looking at areas where efficiencies can be improved, either through direct cost savings or improved outputs, or investments that completely change existing management systems. The Covid restrictions have expanded the use of interactive meetings in conjunction with/replacing on-farm visits, which allows advice to continue to be given while minimising risk (if broadband speed is up to scratch!)

Further rounds of existing schemes also allow farmers to have funded investments in both field and farm infrastructure as well as capital items to improve stock management. Rather than taking the opportunity of funding and spending vital cash just because the opportunity is there, it is important to consider how best to you use the funds available and assess what the investment will do for your farm going forwards. The following points should be considered when investing:

Small Investment Items

- *How long is the capital item expected to last? - depreciate the cost over the expected lifespan related to the specific enterprises it is used for.*
- *Will it save or create additional labour requirements?*
- *Is monitoring equipment really going to be used going forward or just a flash in the pan?*

Farm Infrastructure Items

- *Budget the cost savings and/or additional output to ensure return on capital invested is worth the investment.*
- *Does the investment simplify or complicate the system? Extra complications create extra costs.*
- *How are you going to fund your contribution of the investment?*

With cost of borrowings at a new low, for some businesses it is an opportune time to expand enterprises and the use of grants can aid this, as long as the business has a strong profit track record to be able to secure any additional borrowing. The last 365 days shows that anything can happen, and now is the time for common-sense decisions that will stand your business in good stead for the future.

Contributed Article - **Farm Woodland**

JOHN LOCKHART AND
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When placed in context of the challenges posed by the Covid-19 pandemic of the last six months, the 2019 election now seems a lifetime away. However, despite all the distractions, woodland creation, the environment, and climate change remain at the heart of the Government's policy agenda.

The pandemic will pass, but trees and woodlands will continue to play an important part in our future. The consultation on the England Tree Strategy sets out the range of benefits that woodlands offer including carbon capture, biodiversity, water management, timber and energy production, and recreation.

Planning for the Future

The Strategy looks to achieve a step change in woodland creation and improving management of existing woodlands. It is anticipated that it will affirm the Government's tree planting commitment of increasing planting to 30,000 hectares per year across the UK. If this is to be delivered, it will require Government to work closely with devolved administrations, communities and landowners in both the public and private sectors.

With the emerging Agriculture Bill 2020 and our departure from the EU at the end of the year, we will see fundamental changes in land management as farmers and landowners adapt to the loss of production subsidies, accompanied by a refocus on the delivery of public money to support public goods.

> ***"The long-term opportunities that woodlands present are substantial, ensured by their longevity, and ability to deliver against a vast range of natural capital benefits such as carbon sequestration, water quality, flooding, landscape, biodiversity, health and well-being and air quality."***

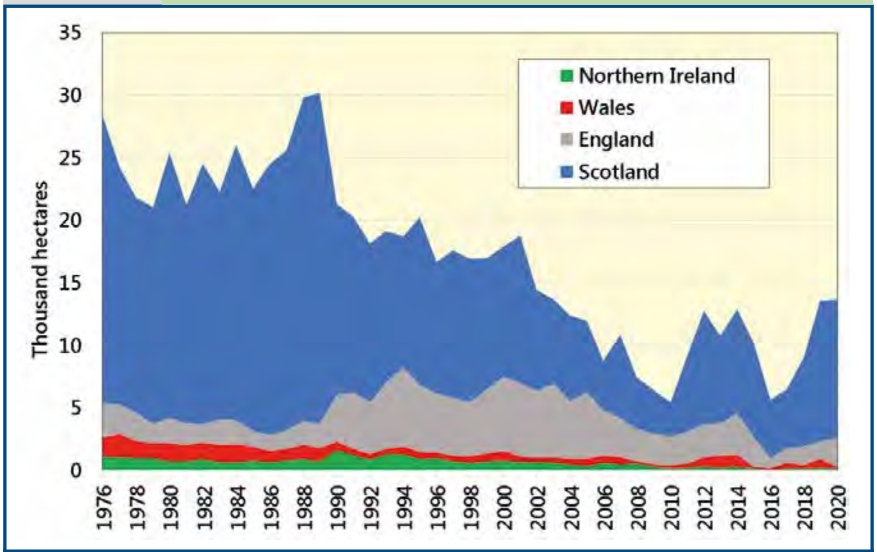
The Environment Bill is also set to influence policy with the concept of Biodiversity Net Gain, becoming a legal requirement. This would see a mandatory requirement for all developments to deliver a 10% net gain in biodiversity. Tree planting, whether onsite or off, will be a key tool in meeting this commitment.

Forestry and trees in their widest sense are now seen as possibly the most important element in helping address the challenges of climate change, air and water quality, carbon capture, recovering nature, and health and well-being. We are seeing a massive increase in interest in woodland management and tree planting, from both within the sector and outside. Many landowners and other stakeholders are now looking at woodlands as a new business opportunity.

Learning Lessons from the Past

After a steady decline dating from as far back as the 12th Century, woodland as a percentage of land area increased in the 20th Century. This was inspired by a realisation of the importance of a sustainable timber resource after two World Wars and the subsequent establishment of the Forestry Commission as part of the 1919 Forestry Act. However, despite this upward trajectory, tree-planting and proactive woodland management, especially in England, is still woefully short of what's needed. In fact, 101 years after the establishment of the Commission, England is looking to learn lessons from Scotland, where the sector has successfully both challenged and supported leaders in Government and the Forestry Commission to make tree-planting objectives a reality. It is clear that, without similar strong leadership and collaboration between Government and the forestry sector, the ambitious plans in England will not be achieved.

Figure 24 **New Tree Planting in the UK – 1976 to 2020**



Source: Forestry Commission

Short-term Assistance, Long-term Gains

A significant barrier to businesses investing in woodland is the fact that it is a long-term commitment, generally considered to be a permanent change of land use. Forestry, woodland and trees across the majority of the lowlands, were, and still are, seen as a marginal business activity at best, with most owners content with achieving little more than covering their costs. For new woodlands, returns from timber sales are far into the future; and with high capital costs associated with establishment, returns are poor and highly unpredictable.

Current grants, whilst significant, have not been sufficient to overcome these barriers at any real scale. Funding that is simpler to access and can be supported by private investment through a range of blended finance models will be critical to effect real change. However, the long-term opportunities that woodlands present are substantial, ensured by their longevity, ability to deliver against a vast range of natural capital benefits such as carbon sequestration, water quality, flooding, landscape, biodiversity, health and well-being and air quality.

Woodland Creation – Where to Plant?

A key consideration is finding the right land to plant on. Land suitable for woodland creation is often in competition with better-understood alternative uses, some of which may yield higher short-term gains such as energy crops, development, food production, biodiversity offsetting and rewilding.

It doesn't make economic sense to use our best and most versatile agricultural land; but equally we need to avoid woodland creation impacting areas of high biodiversity or environmental value. The focus therefore needs to be on those areas of land where profitable farming has relied on production-focused policies and support funding. For example;

- *low-grade arable and temporary grassland;*
- *marginal upland farmland;*
- *ex-mineral restored sites; and*
- *historic landfill sites (which surprisingly account for some 0.85% of land area in England and Wales).*

Historically the loss of flexibility of woodland as permanent land use change has resulted in a significant capital depreciation. However, the right planting on the right land for the right reasons may see capital values increase, especially if the real natural capital values become recognised. As well as the land itself, a flexible approach is needed for tenure, with long leaseholds, pie crust leaseholds and joint venture/share (tree) farming all being possible options.

We are also seeing agro-forestry becoming a real option with fast growing forestry crops, such as Paulownia, offering opportunities for enhanced returns and restoration of soil structure and integrity.

What are the Real Costs?

It is always important to understand the critical requirements for woodland establishment. It is a crop the same as any other and good preparation and implementation are critical to ensure effective and cost efficient delivery, in particular:-

- *woodland design and Environmental Impact Assessment;*

- *supply of suitable plants of appropriate provenance, quality and resilience;*
- *protection and vermin control;*
- *ground preparation and effective planting; and*
- *maintenance and aftercare, including disposal of plastic tree guards.*

It will also be critical to undertake effective and realistic budgeting, taking account of potential future risks from pests and diseases, climate change etc.

What Revenue Streams Might Exist?

Whilst Government's key focus is on expanding our woodland resource, it is equally important to give consideration to the existing woodlands and trees, which demonstrate the pathway that our new woodlands will follow in the coming years. For too long woodlands have been considered the poor relation in comparison to other property assets, and this needs to change if the Government's targets are to be reached. So how might this be achieved?

Timber: The fundamental function of woodlands is the production of timber; whether for construction, fuel or high-quality furniture, timber is a uniquely sustainable product. Recent years have seen significant increases in timber values that have 'opened the door' for many historically unproductive woodlands to be brought back into profitable, functional and sustainable management.

The UK has experienced a rise in the value of timber over the past three years, albeit over a bumpy path at times, particularly during 2018 where prices increased by 33% on some products. This was then brought into check in 2019 as European supplies increased due to wide scale 'sanitation felling' from insect infestation. Prices are on the increase once more, but on a more sustainable level than we saw two years ago.

This increase in prices can be explained by one of the simple economic model of supply and demand. Currently there is considerably more demand than supply and as a result, prices have been increasing. The UK still remains the world's second largest importer of timber, with only China ahead of us. As a result, the timber trade is heavily influenced by the exchange rate. With the Pound currently weak it is making imports far more expensive, allowing UK growers to remain competitive.

Markets are also becoming more diverse. This is particularly the case concerning woodfuel. Traditional firewood has seen prices increased from £2 per tonne in 1999 to £30 per tonne today, as a result of over 150,000 new wood burning stoves going into people's homes every year. There is high demand for biomass/chipwood needed to power our modern combined heat and power plants, and this particular market is now taking timber that only a couple a years ago was considered waste.

The key to maximising profit is making sure the grower finds the right market for the right part of the tree and is constantly looking for the emerging markets as technology and globalisation progresses. For example, the UK now exports white woods such as ash to Vietnam for internal joinery and poplar to Egypt in order to feed its plywood board manufacturers.

Carbon: Accountability around carbon emissions was finally taken seriously when plans for a third runway at Heathrow were rejected by the Court of Appeal in February on the grounds that the proposals did not adequately incorporate the Government's legal commitment to net zero. Forestry is the first sector with established carbon accounting. Under the Woodland Carbon Code, woodland creation now has a clear pathway to revenue. In addition, the Woodland Carbon Guarantee scheme is offering the prospect of realistic returns for sequestered carbon, with offers being made under the first two rounds in the region of £24 per tonne CO_2 and £19 per tonne CO_2 respectively.

Water and Flooding: As recent history has shown, flooding is a major issue across the UK. As well as providing natural flood management, the planting of trees can also help reduce soil erosion and nitrate pollution. Some large-scale woodland projects are now in the pipeline with partners working closely with Local Authorities to address water quality issues across key catchments.

> ***The right planting on the right land for the right reasons may see capital values increase, especially if the real natural capital values become recognised.***

Biodiversity: As noted earlier, Biodiversity Net Gain was created to 'address the hidden costs of development', with the Environment Bill proposing that developments be required to provide a 10% gain in biodiversity from the baseline figure. As a long-term land use, new and existing woodlands can deliver real biodiversity benefits more securely than other habitat creation models that will only be secured for 30 years.

Landscape, Health and Well-being: Woodland creation offers a unique opportunity to create and restore beauty to our landscape. In turn, this enhances landscape recovery, benefits air quality and improves physical and mental health through public access to green spaces – something which has become a key priority during the current Covid-19 crisis. The tangible value that access to high quality green spaces offers society in supporting both our physical and mental health is now recognised. Woodlands, both new and existing have an important role to play in this.

Woodlands – a New Business Opportunity?

The creation and preservation of woodland is a long-term commitment. However, we believe we are closer now to a position where the true value of the benefits that woodland bring to society is properly understood. If we wish to secure these benefits for both our future and that of coming generations, we need to ensure that these benefits are supported by Government, based on their real values. Achieve this and we will see woodlands become a real and sustainable part of rural property businesses, delivering a greener future to which we all aspire.

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