

# AgriMatters

AIB supporting the Irish Agricultural Industry



SUMMER/AUTUMN 2013



Launching the Irish Grassland Association Dairy Summer Tour 2013 are (L to R) Deirdre Hennessy, President, Irish Grassland Association; Kieran Hearne, host farmer; David Kirwan, host farmer and Tadhg Buckley AIB Agri Advisor. Full details of the event are available on [www.irishgrassland.com](http://www.irishgrassland.com)



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## Welcome to the Summer/Autumn edition of *Agri Matters*

### Michael Dowling, AIB Agri Strategy Consultant

In this edition of *Agri Matters* we look at the economy as a whole and see some tentative signs of recovery but with a realisation that there is a long way to go.

From an agri point of view, this has been an extraordinary year so far. The first four months saw the continuation of the unusually wet conditions that created such difficulties in the second half of last year and caused a severe fodder crisis through the winter and spring. The consequences of those conditions for farm income are graphically set out in Thia Hennessy's article on the 2012 National Farm Survey. From early May, however, the weather turnaround, combined with a surge in milk prices and continuing very strong beef prices, has dramatically changed the situation on the ground, so that we now expect that farm incomes this year will very likely rebound towards the record levels of 2011. Fodder should not be the same problem it was last year and early this year. We have, however, included a copy of the Teagasc fodder budgeting worksheet, which we would encourage our readers to complete.

Weather conditions of a different kind are emphasised in the article by Oliver Quigley, a New Zealand farmer, on the severe consequences for farmers there of the prolonged drought, which has piled pressure particularly on the fairly large number who are very heavily indebted. The article underlines the action taken by farmers themselves, processors, Government, tax and public health authorities and the banks, to alleviate the situation.

The period since 2006 has underscored what many have been predicting for some considerable time – that the running down of EU market supports is exposing the agri sector to much more market volatility. In his article Tadhg Buckley, AIB Agri Advisor discusses volatility and what action farmers can take to mitigate its effects.

By far the most significant event of the year was the agreement at EU level on CAP reform. The centrepiece of the reform is the revised direct payment system with some redistribution of aggregate payment levels between Member States and some movement towards greater convergence of payments to farmers at national or regional levels. As expected the final decisions moved in the direction of the original Commission proposals but with substantial adjustments. We raised the question in our last edition as to whether those decisions would offer sufficient flexibility to meet Ireland's negotiating aims, which were to create a more balanced system but one where more productive farmers were not unduly penalised. As is clear from the article on this subject, by and large those aims have been achieved and the final shape of the new arrangements here will be completed by decisions to be taken nationally in the autumn. The overall package also included agreement on the rural development policy up to 2020 and some changes in market management measures, including the phasing out of sugar quotas by 2017. The Minister and his civil service team are to be congratulated both on the narrow outcome as it relates to our own negotiation aims and, more widely, on steering through a tripartite agreement between the Council, the European Parliament and the Commission on what was a very complex dossier.

Finally, we acknowledge Matt Dempsey's great contribution to the agri sector in his stewardship of the Irish Farmers Journal and, more generally, by including in this edition an article in which he reflects on the changes in the agriculture and food sector during the long period of that stewardship.

We wish all our readers and their families an enjoyable and productive year.

Michael Dowling  
AIB Agri Strategy Consultant

## Our Agri Advisor Team



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# ECONOMIC OUTLOOK

The latest data on the Irish economy (Table 1) shows that GDP growth was higher than originally reported for 2011 at 2.2% (previous estimate was 1.4%). With little change to the absolute level of GDP in 2012, the higher base for 2011 meant that there was a significant downward revision to GDP growth last year, from 0.9% to 0.2%.

Thus, after a marked pick up in growth in 2011, the recovery stalled last year. The reason for this was a sharp slowdown in export growth from 5.4% in 2011 to just 1.6% last year. Two factors are at work here. First, a marked fall in exports from the pharmaceutical sector following the expiry of patents on a number of key products manufactured here. Second, the EU economy, which takes two-thirds of Irish exports, went back into recession last year.

These two negative factors remained in place in the opening quarter of this year. As a result, goods exports, which are dominated by the pharmaceutical sector, were down by almost 10% on year earlier levels. Meanwhile, the year-on-year growth in service exports slowed to just 1.3% in the first quarter of 2013, down from 9.4% a year earlier.

Given that exports have been the sole source of growth, the weakness in the sector has had a very negative impact on GDP growth, returning the economy to recession since mid-2012. However, the data also show that, on a GNP basis, the economy continues to grow. GNP takes income flows into consideration and the fall in exports has been offset by lower profit repatriations by multi-nationals.

In terms of the domestic economy, at first glance, the latest national accounts data suggest that the domestic sector remains in deep recession. It contracted in both the final quarter of last year and opening quarter of 2013, leaving domestic spending down 2.3% year-on-year.

However, when one strips out the highly volatile investment in aircraft component, which has little to do with the domestic economy but reflects the presence of a large aircraft leasing industry here, the figures show that the domestic economy has largely stabilised over the past year, with output unchanged on a year-on-year basis.

On the labour market front, the data has improved in the last year. The latest official figures, which cover the period up to the end of the first quarter of this year, showed that the number employed was higher by over 20,000 from a year earlier. The positive trend to employment growth, as well as net outward migration, is helping to put downward pressure on the unemployment rate, which has fallen to 13.6%, down from a peak of over 15%.

Meanwhile, the housing market is showing signs of stabilisation over the past year. The number of mortgage approvals and housing transactions has risen, while the decline in house prices and house building appears to be bottoming out. Meanwhile, the budget deficit continues to decline, with tax receipts broadly in line with target, both in 2012 and the first half of this year.

From an agricultural perspective, while based on CSO estimates, the volume of production in the sector was virtually unchanged in 2012, farm incomes declined as a result of higher input costs associated with the bad weather and lower milk prices. This situation extended into the first half of this year, with increased feed and fodder usage, due to the

bad weather and further increases in some farm input prices, having a dampening impact on income levels. The position has generally improved over the past couple of months due to buoyant cattle and milk prices, some lowering of input costs and improved weather.

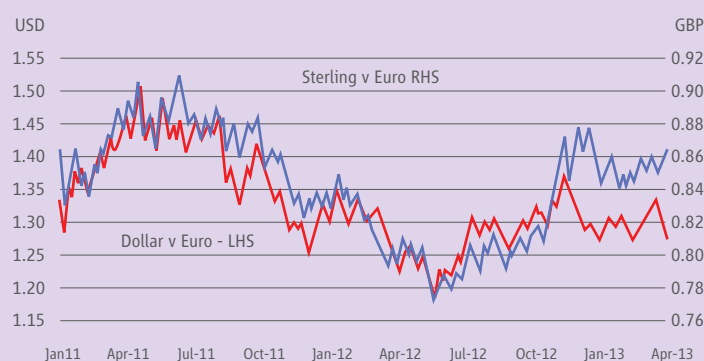
Overall, exports need to strengthen again for the recovery in the Irish economy to gain traction. The omens are promising, with signs of an improvement in the European and global economy, as well as some pick up in output from the pharmaceutical sector recently. Thus, while 2013 will be another year of weak growth in Ireland, the pace of activity should pick up thereafter.

Table 1: Economic Forecasts – Ireland				
Annual % Change Unless Otherwise Stated				
	2011	2012	2013 (f)	2014 (f)
Real GDP	2.2	0.2	0.5	2.2
Real GNP	-1.6	1.8	3.0	1.7
Consumer Spending	-1.6	-0.3	-1.0	0.5
Government Spending	-2.8	-3.7	-2.5	-2.0
Fixed Investment	-9.5	-1.0	-3.0	5.0
Exports	5.4	1.6	0.5	3.5
Imports	-0.4	0.0	-0.5	2.0
HICP Inflation (%)	1.1	2.0	0.8	1.3
Unemployment (%)	14.6	14.7	13.6	13.2
General Govt. Deficit (as % of GDP)	9.1	7.6	7.2	4.8

Source: CSO, AIB Economic Research Unit Forecasts  
(f) = forecast

On the currency markets, as we reach the halfway point of the year, the euro has put in a solid six months (Figure 1). While the eurozone debt crisis was a key factor impacting on eurozone financial markets in 2011-12, its negative influence has waned, with the euro becoming more immune to these difficulties. In fact, so far this year, the euro has displayed surprising resilience, in the context of an economy that is still contracting and a Central Bank that cut interest rates in May and retains an easing bias.

Figure 1: Relative performance of the Euro against the US Dollar and Sterling



Source: Thomson Datastream

Overall, the euro could continue to trade in its current \$1.27-1.33 range versus the dollar. We also envisage a continuation of range bound trading for the euro sterling currency pair, within an 83-87p band.

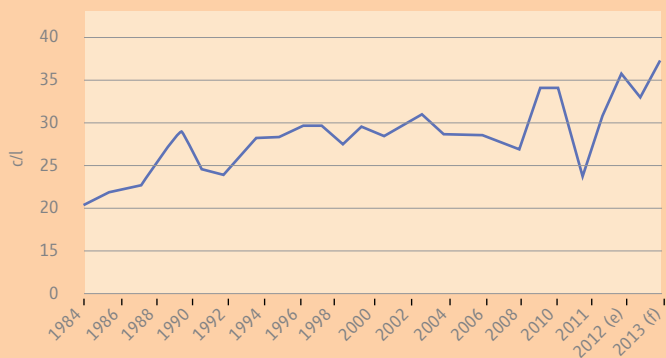
## Market Review

Last year was a very difficult one for most Irish farmers, despite output prices in many sectors being extremely strong. Input prices – especially feed, fertiliser and energy – at close to historically high levels, combined with the effects of the appalling weather conditions in the second half of the year, led to a sharp drop in farm incomes compared to the very high levels achieved in 2011. This is clearly illustrated in Thia Hennessy's article on the 2012 National Farm Survey (and confirmed in the latest CSO figures which show a drop of about 10% in farm income after interest and rents are taken into account). Thia's article also confirms, however, that, despite that income drop, average farm incomes in 2012 were relatively high compared to the previous seven years. The depressing effect of the weather conditions made it feel very much worse.

Despite the continuation of the wet weather throughout the spring, it looks as if there will be a sharp rebound in farm incomes this year. The onset of more normal summer weather had seen a big improvement in grass growth over the past two months. Milk prices have surged since April and beef prices have stayed at very high levels since the end of last year. Input costs have stabilised and should begin to fall in the second half of the year. Fodder should not be the problem it was last year and early this year but there could still be a fairly tight situation in early spring 2014.

**Milk** prices began to rise in the autumn of last year and that trend continued into this year and indeed accelerated in recent months. In May, the price stood at 37/38c/l (VAT inclusive), probably the highest summer price ever recorded. It is likely that the average price for the year will be 37c (actual butterfat), again a historic high (Figure 2). High feed usage and prices in the winter and spring will have added to input costs but, nevertheless, dairy farm incomes should be substantially up on 2012. Milk deliveries are likely to increase by some 2.5% in the calendar year, making it very likely that the quota situation in the milk year will be very tight.

Figure 2: Manufacturing Milk Price



Source: CSO and AIB estimate 2012 and forecast 2013

**Beef** prices at the end of June stood at €4.75/kg (R3 steers) for quality assured in-spec cattle. This exemplifies the very strong prices that have applied in the market since the autumn of 2012. Beef prices peaked in 2008 and dropped off up to late 2009. Since then there has been an almost continuous rise to a level well above 2008 or anything seen before that (Figure 3).

As is clear from Figure 4, the Irish steer price was (end June) on a par with prices on the Continent but maintained its traditional position below prices in Great Britain (although heifer prices in Ireland were in past weeks higher than UK prices).

Supplies which were very tight all last year are rising considerably this

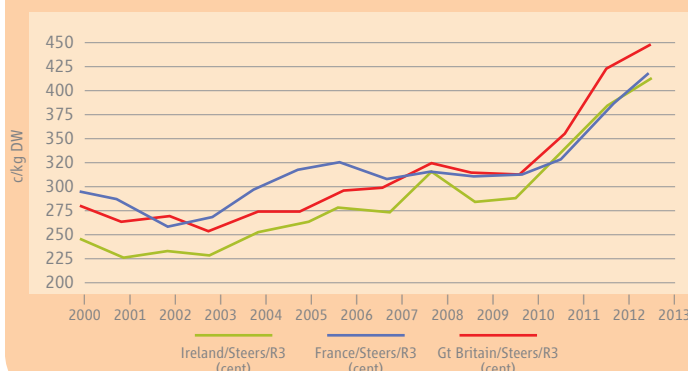
year, with slaughtering up 10% in the first five months and live exports (particularly calves) also up, admittedly from a very low base. Throughput should be up by more than 10% over the year as a whole and, while prices have started to weaken somewhat, they should remain above the average level of 2012 and well above the levels of earlier years. Calf and weanling prices are, however, down by varying degrees which may dilute some of the benefit for cattle rearers but improve margins for those operating further up the chain.

Figure 3: Irish R3 Steer Prices (Quarterly)



Source: Bord Bia

Figure 4: Cattle Prices



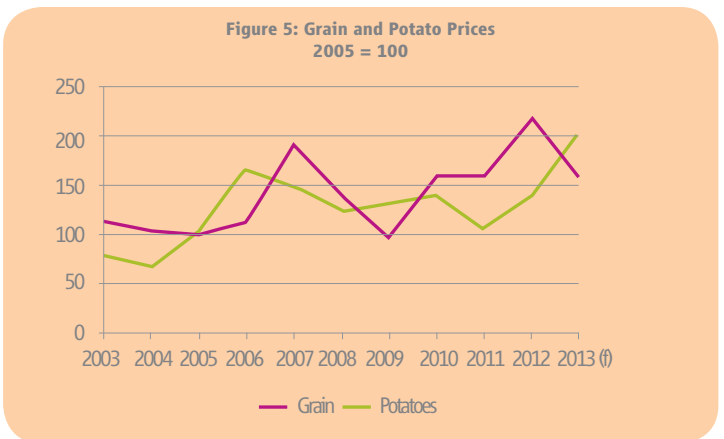
Source: Bord Bia

**Sheep** prices are back over 3% year to date (June) but, in recent weeks, are running well ahead of last year. They are, more or less, level with prices in the UK but, as is normal, well behind French prices. Over the year, as a whole, we would expect prices to be 5% or so better than in 2012. Slaughtering to date are up by about 16% but the rate of increase has moderated over the past couple of months. Nevertheless, for 2013 as a whole throughput should increase by over 10%.

Irish **pig** prices are up by over 10% year to date but the rate of increase had fallen to about 3% a week by the end of June. Irish prices are running ahead of Danish and Dutch levels but well behind prices in the UK. In the year, as a whole, we would expect prices here to be some 5-10% up on 2012 levels. Prices are, however, lower now than earlier in the year and this, together with continued high feed costs, has put renewed pressure on the profitability of many producers. Those towards the top end of the efficiency scale would appear to be still operating profitably. Furthermore, there is the prospect of some price increases in the second half of the year and of lower post harvest feed costs.

**Grain** prices rose dramatically at harvest time last year, with the result that prices in 2012 were about 35% above the previous year's relatively high levels. Prices remained at, or above, those levels for most of the period since. There have been clear signs recently that prices are weakening in anticipation of an abundant harvest this year, although there are still some uncertainties arising from earlier weather events. As a tentative estimate we would put the drop in the price of new season grain at about 25% to 30%. This would still leave prices at or a little below the 2011 and 2010 price levels and well above the levels of the previous decade. As soya prices are also falling, the outlook for feed costs would appear to be favourable in the short to medium term and the likely production response could see some pressure on milk and beef prices going forward.

**Potatoes** have been even more volatile than grain prices over the past 10 years (Figure 5). Last year saw a substantial rise (30%) in potato prices compared to 2011 but this tells only part of the story. Prices post harvest were almost 180% higher than in the previous harvest. These price levels continued into this year when, for example, April prices were 200% higher than a year earlier. At this stage it is difficult to predict the outcome of the forthcoming harvest as much will depend on harvesting conditions (and prolonged dry weather could affect yields) but prospects look promising, even if some easing of prices can be expected.



Source: CSO and AIB forecast

All in all, the farm income outlook for this year looks quite good. Output prices are, and should remain, strong. Feed prices are very likely to moderate, energy costs are a little lower and fertiliser prices seem to have peaked. Most importantly weather prospects look more favourable. Even allowing for the extra costs incurred earlier in the year due to the fodder crisis, we would expect farm incomes (after interest and rents) to rise by between 5% and 10%. This would still leave them below the 2011 level but ahead of earlier years.

#### Correction to Spring 2013 edition of Agri Matters.

An error appeared in the 'New Zealand Study Tour' article in our printed edition. The differential in profit per hectare between the top quartile group of farmers and the bottom quartile group of farmers, as quoted by Dairy NZ in 2011, should have read €2,020/hectare and not €330/hectare as was stated in the article. The revision has been made to our online edition available on [www.aib.ie/farming](http://www.aib.ie/farming)

## Recent Appointments



### Tom Hayes

Minister Tom Hayes TD, a Tipperary native, was appointed a Junior Minister at the Department of Agriculture in June last, with special responsibility of Horticulture, Forestry, the Greyhound Industry and Food Safety. Currently the sole Government TD in the Tipperary South constituency, Tom began his political career in 1991 when elected to Tipperary South Riding County Council. Acting as Fine Gael Seanad spokesperson on Agriculture in 1997; Tom has subsequently been appointed Fine Gael Deputy Spokesperson on Agriculture and Food; Deputy Spokesperson on the Environment, with Special Responsibility for Heritage and Rural Affairs; Chairperson of the Fine Gael Parliamentary Party; Chairman of the Joint Administration Committee; and Chairperson of the Oireachtas Joint Committee on Transport and Communications during his term of office. Married to Marian with three sons (Padraic, Ronan and Cathal), Tom enjoys GAA, horseracing, greyhound racing, rugby and traditional music.



### Kieran O'Dowd

Kieran O'Dowd was elected president of Macra Feirme in May 2013. Kieran, a Sligo native married to Caroline Marren - herself an active Macra member - first joined Macra in 2004 and has held various positions at club, county and national level. He was National Council Representative for Sligo in 2007; elected to the National Executive in 2008; elected National Chairperson in 2009, and served as National Treasurer from 2009 to 2011. He represents Macra na Feirme on the board of the National Youth Council of Ireland serving as Treasurer of the National Youth Council of Ireland from 2009 to 2011. Presently Kieran practises as a barrister on the Midlands Circuit and also works part-time in the Michael Coleman Heritage Centre as public relations and events organiser.





July 2013

**HELP IS  
AVAILABLE**  
CONTACT YOUR  
LOCAL ADVISER

## Take action now...

### ...if you are short of fodder.

1. Start planning now. Those that acted earliest last year came through the spring more easily.
2. Increase the fodder required by 10-20% to replace depleted silage stocks.
3. Once you have at least 50-60% of your winter silage requirements, you have options available.
4. Silage dry matters can vary. The standard is 200kg DM per tonne of pit silage and 180kg per bale. These are typical with a maximum of one day wilting. If DM is higher, take this into account.
5. There is no single strategy to deal with the shortage. A combination of actions will be needed to help you deal with the problem:
  - a. Maximise grass growth on the farm over the next few months: apply 20-30 units of nitrogen (N) to grazing ground and remove surplus grass as bales, where possible.
  - b. The alternative feed options include:
    - i. buying silage – standing crops of grass for silage or baled/pitted silage;
    - ii. buying ration to fill the gap;
    - iii. growing forage crops such as rape;
    - iv. buying alternative forages such as maize silage, whole crop cereal silage, or fodder beet; or,
    - v. buying cereal grains and store.
  - c. Match demand with available winter feed:
    - i. consider marketing cull cows (scan cows early);
    - ii. planned marketing of store cattle; and,
    - iii. put finishing cattle on meals and minimal silage.
  - d. Examine the options carefully. Cost is important but other factors also need to be considered, including the risk of poor yields/quality, the need for storage/handling facilities, the cost of balancing for protein and minerals, the labour input, cash flow implications and feed space requirements.
6. Don't panic buy feedstuffs to fill the gap. Talk to an adviser before making your decision.

Maximise grass growth for both silage crops and grazing.  
A kilo of N applied in July and August will deliver up to 35kg of grass DM.

# FODDER BUDGETING SHEET

## Farmer details

Name	Enterprise
Herd number	Land type
County	

## SECTION 1: What fodder is required on the farm?

Animal type	A No. of stock to be kept over winter	B Number of months	C Pit silage needed/ animal/month	Total tonnes of silage needed – multiply AxBxC
Dairy cows			1.6	
Suckler cows			1.4	
0-1 year old			0.7	
1-2 year old			1.3	
2+ year old			1.3	
Ewes			0.15	
Total tonnes needed				Tonnes <input type="text"/> X
or				or
Total bales needed (tonnes multiplied by 1.1)				Bales <input type="text"/> Y

## SECTION 2: How much silage is in the yard and/or to be harvested?

Farms with pit and bale silage	A	Pit silage – currently in the yard <sup>1</sup>	<input type="text"/>
	B	Pit silage – to be harvested (acres multiplied by 7t/ac)	<input type="text"/>
	C	Total pit silage (A+B)	<input type="text"/>
	D	Bales – in the yard/to be harvested	<input type="text"/>
	E	Bales, converted to equivalent of pit silage (Multiply D by 0.9)	<input type="text"/>
	F	Total silage (C+E)	<input type="text"/> F
Farms with bale silage only	A	Bales – in the yard	<input type="text"/>
	B	Bales – to be harvested	<input type="text"/>
	C	Total bales (A+B)	<input type="text"/> C

<sup>1</sup> Pit silage (length x breadth x settled height) metres ÷ 1.35 = tonnes (t) equivalent.

## SECTION 3: Surplus or shortage?

Surplus or deficit	Using pit and bales Deficit in tonnes (F-X)	Using bales only Deficit in bales (C-Y)
	<input type="text"/>	<input type="text"/>
What's the % deficit? (Deficit/X (or Y) *100)	<input type="text"/>	<input type="text"/>

\* If you are using alternative feed sources, please contact your adviser.

## CAP Reform

The EU has, at last, reached agreement on the broad outline of the CAP to apply from 2014 to 2020. As expected it follows the general lines of the Commission's original proposals but with very significant adjustments, not least in the extent to which flexibility is allowed to Member States in implementation. The latter element means that important issues have yet to be decided nationally and these decisions are not likely to be taken for some months. The following paragraphs outline what has been agreed at EU level.

### Direct Payments

Overall the Irish national budget for the Single Farm Payment (SFP) is reduced to €1.217m in 2014 from €1.230m (net of modulation) in 2013. This 1% cut is a function of the overall EU budget decisions. There are a number of specific allocations which must be made from this national budget which will reduce the general level of single farm payments:

- Up to 2% is to be used for a young farmers' scheme; and,
- Up to 3% is to be used for the national reserve.

These allocations, of course, stay within farming. The national reserve is to be used to give entitlements to young farmers, farmers commencing agricultural activity or to those in certain other specific circumstances. The amount set aside for the young farmers' scheme is to be used to top up by 25% (for a maximum of five years) the basic payment allocated to farmers under 40 years of age starting up, or who started up within the previous five years.

There are two other allocations which must generally be made:

- A crisis reserve of 1% to deal with the consequences of market disturbance. This is repaid to farmers each year if not used during the year.
- Under financial discipline rules there would be linear cuts on single farm payments above €2,000 to avoid breaches of the financial sub-ceiling for direct payments and market management measures under Pillar 1 (this in fact begins in 2013 in which year the threshold is €5,000; the €2,000 threshold kicks in for 2014 and subsequent years).

The extent, if any, of the latter allocation would be decided each year in light of the foreseen budgetary position. The deduction proposed for 2013 is 5% (had the €2,000 exemption limit applied this year the percentage reduction would have been something over 3%).

### Redistribution of Direct Payments

This is the centrepiece of the reform. There are two options. The first is the original Commission proposal to move to a flat rate payment per hectare at national or regional level by 2019. The second is partial convergence by 2019. This was first mooted by Ireland (and, therefore, one assumes will be applied here) and what has been agreed as this option is a slightly modified form of the Irish proposal. The details are:

- Farmers with payments below 90% of the national average payment per hectare have their payments raised by one-third of the difference between their current payment and 90% of the national average. This mirrors the method for redistributing aggregate payments between Member States;
- There is a stipulation that where this does not result in a payment equal to at least 60% of national/regional average payment per hectare the payment will be raised to that minimum level;
- These two measures, to be introduced gradually from 2015 to 2019, will be financed by reductions to payments above the national average payment per hectare. Member States have flexibility on how payment reductions are to be applied to those above the average and can in addition apply an optional maximum 30% loss on convergence;

- Some 30% of the national SFP budget is to be set aside for payments for meeting a number of greening conditions. This can be either a uniform flat rate payment per hectare in the Member State or region concerned or a variable premium equal to 30% of a farmer's individual payment (this is most likely the option to be adopted in Ireland); and,
- There are two further optional redistributive elements. Member States may apply a maximum payment per hectare, which would reduce the payments for all farmers with higher payments per hectare than the maximum. In addition, they may use up to 30% of the national or regional SFP budget to pay an additional premium on up to 30 hectares of each farmer's eligible holding or up to the national average farm size, if higher (32ha in Ireland). The last mentioned measure would, of course, result in a reduced payment on hectares in excess of the area topped up.

Only farmers paid in 2013 can be automatically allocated new entitlements and the number of entitlements to be allocated is to be equal to the number of eligible hectares declared in either 2013 or 2015 (to be decided by Member States).

### Active Farmers

Payments are to be made only to active farmers. To define active farmers Member States are to set minimum activity level for areas 'naturally kept in a state suitable for grazing or cultivation'. Member States may also exclude from payment those for whom farming is an insignificant part of their economic activity. They are required to exclude airports, railway services, waterworks, real estate services and permanent sport and recreational grounds from payments unless the operators concerned can show that they have genuine farming activity. Member States may add to this list.

### Coupled Payments

Member States may use up to 8% of their annual SFP national budget to provide coupled aid for specific livestock or tillage sectors and a further 2% for aid for protein crops. Ireland did not take up the option of coupled aid in the existing SFP system but now has again the option to do so.

### Small Farmer Scheme

This is an optional scheme for Member States. Where implemented, small-scale farmers can opt for a simplified scheme qualifying for payments of between €500 and €1,250, under which they would be exempt from greening controls and face less stringent cross compliance requirements. Up to 10% of the national ceiling can be used for this scheme but, if applied in Ireland, it would be likely to require less than 1% of the budget.

### Greening

Payment of 30% of the direct payment is contingent on compliance with three greening criteria. In the convergence model likely to apply in Ireland this will be calculated as 30% of the individual's own payment rather than a national or regional flat rate amount per hectare.



The three criteria to be observed are:

1. **Crop Diversification:** Farmers with between 10 and 30 hectares of arable land must cultivate at least two crops; those with over 30 hectares must grow at least three crops. The main crop cannot cover more than 75% of the area and no crop can cover less than 5%. There are exemptions from the crop diversification requirement for farmers with:
  - (a) less than 10 hectares of land;
  - (b) over 75% of the holding under grassland (permanent and temporary); or
  - (c) over 75% of the arable land under temporary grassland, provided the remainder of the holding is less than 30 hectares.
2. **Permanent Grassland:** Permanent grassland must be maintained at national, regional or farm level. A new permanent grassland ratio will be created using 2012 declarations, which will be updated to take account of additional lands declared in 2015. The allowance for the conversion of permanent grassland compared to the reference ratio is 5%. There will be a ban on ploughing of certain designated lands in permanent grassland within Natura 2000 areas where the areas are environmentally sensitive and where the objectives of the Directive require them to be strictly protected.
3. **Ecological Focus Areas:** The requirement to maintain ecological focus areas applies to arable land and only where the holding is 15 hectares or more. If it is, 5% of the arable land must be an ecological focus area, increasing to 7% in 2017 after a Commission report and proposal. Qualifying areas include fallow land, terraces, landscape features and buffer strips, with a weighting matrix in respect of the areas/features

included. As in the case of crop diversification, there are exemptions for holdings having more than 75% in grassland (permanent or temporary), or covered by crops under water, or a combination of both, subject to the remaining land being not more than 30 hectares. There are exemptions also for holdings where more than 75% of the arable land is temporary grassland, fallow, under leguminous crops, or a combination of these, again subject to the remaining land being not more than 30 hectares.

**Equivalence:** A number of actions can be accepted as equivalent to these criteria for purposes of meeting the greening requirements – in particular organic farming and certain measures in agri-environment schemes. Farmers will not, however, be paid twice for undertaking these actions (i.e. payments for the equivalent agri-environment measures will be correspondingly reduced).

**Penalties:** There will be no additional penalty (i.e. beyond loss of the greening payment) for failure to meet the greening criteria in the first two years. In year three the additional penalty will be 20% of the greening payment and 25% from year four.

Direct payments were not, of course, the only elements in the reform package as it included also market support elements and the rural development policy for the next seven years.

**Market Measures:** The agreement included greater flexibility for the Commission to intervene in the market; export subsidies to be used only in exceptional circumstances; opening of intervention to be discretionary; some increase in the beef intervention price percentage; an increase in the



Launching the 2013 Tullamore Show and AIB National Livestock Show were An Taoiseach Enda Kenny; Freda Kinnarney, Secretary, Tullamore Show; David Duffy, Chief Executive, AIB and Rodney Cox, Tullamore Show Chairman. This years Show takes place on Sunday, August 11th in Butterfield Estate, Tullamore.

quantities of butter and skim milk powder to be eligible for fixed price intervention and an extension of the intervention period for these products by one month. From an Irish point of view, the downplaying of export subsidies is of some very limited concern but these have gradually become fairly insignificant and, if there is ever to be a new WTO agreement, they would disappear completely. Perhaps the biggest change from a wider EU point of view is the ending of sugar quotas in 2017.

**Rural Development:** The rural development proposals were outlined in our last edition. The decisions taken were generally along the lines proposed by the Commission. The new policy, to run from 2014 to 2020, will have three main aims - competitiveness, sustainability and the rural economy. It will have six priorities: knowledge, competitiveness, the food chain, ecosystems, carbon and jobs. Member States will be able to frame targeted programmes that pick from a menu within those priorities. A minimum of 30% of the overall budget must, however, be reserved for agri-environment, forestry and disadvantaged area schemes and 5% for Leader. In addition a number of existing type schemes, such as on-farm investment, can still be available and there are new possibilities in terms of insurance and income stabilisation schemes. The overall EU budget for rural development at about €85bn is down by some 12% compared to the 2007-2013 period; Ireland's share at some €2bn (€313m a year) over the seven years is down from about 2.6% to 2.3% of the overall. This remains, however, a reasonable 'take' when compared to our share of EU agricultural land (2.4%), rural and intermediate areas (1.7%) and agricultural output and labour (a little over 1% in both cases).

### Conclusion

There is no doubt that the elements relating to the direct payments are by far the most important parts of the package. Some issues remain to be settled at national level, in particular:

- Will Ireland stick with the partial convergence option?
- If so, how is the 'cost' of convergence to be spread across those with above average payments per hectare?
- Will Ireland apply the 30% maximum loss rule?
- Will we impose a maximum per hectare payment limit?
- Will we use the redistributive possibility of topping up the payments on the first 30 or so hectares?
- Is 2013 or 2015 to be the base year for determining entitlements?
- Will Ireland make use of the coupling provision?
- Will the small farmer scheme apply in Ireland?

The answers to some of these questions would appear to be clear cut. One of the main Irish aims in the negotiations was, while accepting the need to bring greater balance to payment rates, to limit to reasonable levels the loss of income of the more productive farmers. That being the case, then we are certain to stick with the partial convergence method and, it could be argued, should also apply the maximum 30% loss criterion and avoid imposing a maximum payment figure (although, if the latter were applied at, say, €700/ha the cost to those with payments above that figure, and the gain to those below it, would be no more than about €10m). In light of the negotiating aim referred to above, there must be a question mark also over the likelihood of the use of the topping up redistributive element.

The method chosen to distribute the 'cost' of convergence and the minimum payment to the payment bands above the average level and the question of coupling are perhaps the most interesting issues. On the figures available (and they are subject to change in the light of more up to date data), 90% of the average payment is about €240/ha and the minimum payment (60% of the average) is about €160 (when deductions for the reserve, young farmers and the crisis fund are made these figures would become €225 and

€150 respectively). The decisions now taken mean that by 2019 those with payments below the minimum must have their payments moved up to that level and those with payments between the minimum and the 90% figure would have these increased by one third of the difference.

This results in a 'cost' of about €103m which must be recouped from payment levels above €267 (the original Commission proposal would have resulted in a transfer of €280m).

It was originally expected that this would be done on a proportionate basis which would result in graduated reductions in the level of payments above the average along the lines of the following approximate examples:

- Payment of €275 reduced by 2% to €270/ha
- Payment of €450 reduced by 15% to €280/ha
- Payment of €650 reduced by 20% to €520/ha
- Payment of €1,100 reduced by 27% to €800/ha

The final agreement leaves the decision on the method of recoupment to the Member State on condition that it is done in an objective manner. While, in our view, the method is still likely to be the proportionate one, other possibilities are also open, e.g. a linear cut.

The other main outstanding issue is coupling. Following the Fischler reform Ireland took the decision to decouple completely. Some other Member States retained some coupled payments, particularly in the livestock sector. The issue now arises as to whether we wish to follow suit. In particular, it is considered likely that, without some level of coupled payment, the suckler herd is set to contract and, thus, reduce the availability of premium raw material to the beef industry, which, understandably, is generally in favour of coupling. This can, of course, be done only at the expense of reduced payments in the other sectors and in a reversal of policy decisions taken on the introduction of the decoupled system.

Finding a balance on this issue is not easy, but it is something that, together with the other outstanding elements referred to above, must be decided one way or the other to allow the reformed CAP arrangements to be put in place. We would expect that the necessary decisions will be taken in the early autumn after a period of consultation.



Launching the new Teagasc 'Business Planning Workbook' for dairy farmers sponsored by AIB at the Moorepark Open Day were (L to R) Bill O'Keeffe, Conna; Fintan Phelan, Teagasc; Tom O'Dwyer, Head of Dairy Knowledge Transfer, Teagasc; Donal Whelton, AIB Agri Advisor and Michael Crowley, Skibbereen. The workbook is available on the AIB and Teagasc websites.



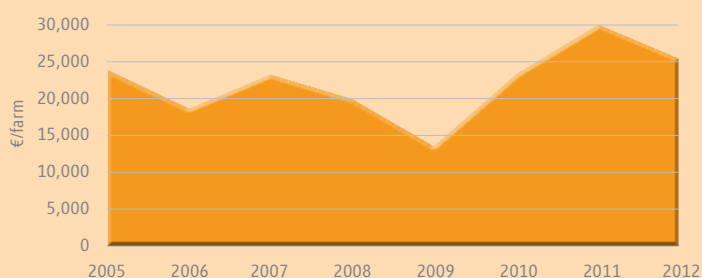
## Farm incomes down 15% in 2012

**Thia Hennessy**  
Head, Teagasc National Farm Survey

In May, the Teagasc National Farm Survey presented preliminary farm income results for 2012. The survey, which has been running for 40 years and collects data on approximately 1,000 farms each year, recorded a 15% reduction in average family farm income in 2012 relative to the previous year. The average family farm income in 2012 was €25,483. The inclement weather was the main driving force behind this reduction. On average, the value of output on farms remained more or less unchanged between 2011 and 2012 but direct costs of production increased substantially. Livestock farms were particularly adversely affected by the very wet summer and early onset of winter with expenditure on concentrate feed up almost one-third on dairy farms.

Although income decreased by 15% in 2012, income was still comparatively high relative to the previous seven years (Figure 6). Family farm income reached unprecedented levels in 2011 and despite the 15% decline in 2012, incomes were still at the second highest level on record since 2005 (a year in which incomes were inflated due to what was in effect a part double payment of some premiums on the switch over to the single farm payment).

**Figure 6: Average Family Farm Income: 2005 to 2012**



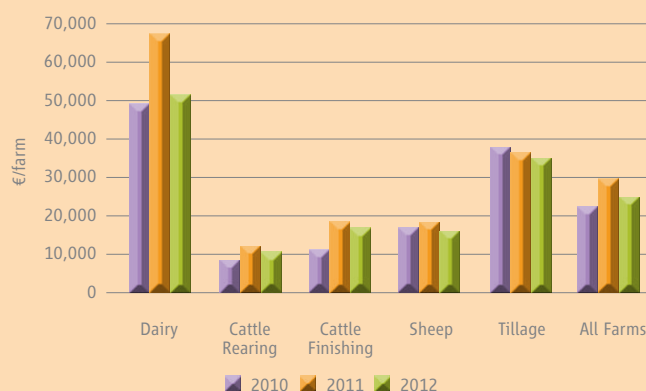
### Income by system of farming

Dairy farming continues to be the most profitable farm business with average incomes far in excess of the other farm systems (Figure 7). On dairy farms, average family farm income fell by 24% in 2012 to €51,648, representing a return to the 2010 level. The impact of the declining milk price, which fell by 9%, was offset by strong cattle prices and overall farm gross output was more or less unchanged in 2012. However, dairy farms were particularly adversely impacted by the weather, and direct costs of production were up 21%.

The drystock sector (cattle and sheep farms) continues to be characterised by a large number of small, low-income farms. Although cattle farm gross output increased in 2012, production costs rose faster and average family farm income decreased by 8% on both cattle rearing and finishing farms.

As with the other livestock systems, gross output levels on sheep farms were more or less unchanged from 2011 to 2012 but increased input expenditure eroded profits. Income on sheep farms fell by 11% on average in 2012.

**Figure 7: Family Farm Income by System of Farming: 2010 to 2012**



Income on specialist tillage farms fell for the third consecutive year and the gap between dairy and tillage farm incomes continued to grow in 2012. Despite significant increases in cereal prices in 2012, the weather adversely affected yields and the value of crop output on tillage farms was down nearly 20%. Production costs did not increase as significantly on tillage farms in 2012 due to the lower importance of livestock and lower expenditure on animal feeds. On average, income on tillage farms fell by 4% in 2012.

### Reliance on Direct Payments

On average, total direct payments per farm, which include the Single Farm Payment (SFP), the Disadvantaged Area Scheme (DAS), the Rural Environmental Protection Scheme (REPS) and other subsidies including the newer Agri-Environment Options Scheme (AEOS), were €20,534 in 2012, comprising 81% of farm income (Table 2). Reliance on direct payments varies considerably by farm system and is highest in the drystock sector. On average, the two cattle and the sheep farm systems incurred a market loss from production. In other words, the revenue generated from the sale of livestock was insufficient to cover the costs of production and the direct payments were used in part to subsidise this loss making production.

**Table 2 : Contribution of Direct Payments to Family Farm Income**

	Total Direct Payments	Share of Income
	€	%
<b>Dairy</b>	<b>22,596</b>	<b>44</b>
<b>Cattle Rearing</b>	<b>15,458</b>	<b>131</b>
<b>Cattle Other</b>	<b>20,793</b>	<b>118</b>
<b>Sheep</b>	<b>19,961</b>	<b>118</b>
<b>Tillage</b>	<b>26,484</b>	<b>75</b>
<b>All Farms</b>	<b>20,534</b>	<b>81</b>

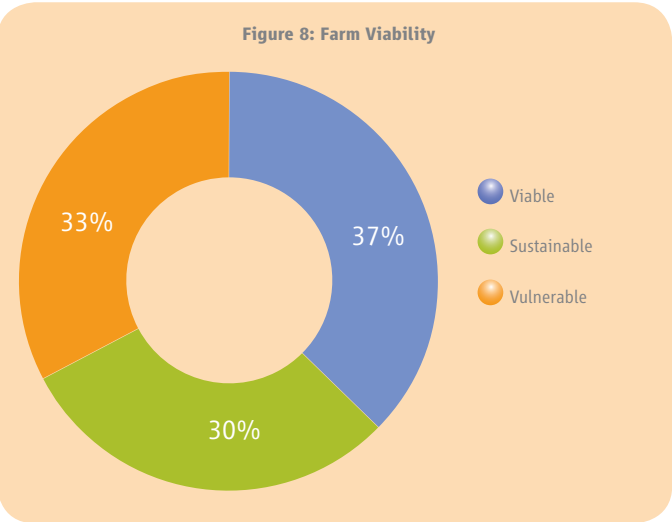
### Viability of Farming

Each year the Teagasc National Farm Survey classifies farms on the basis of viability. Farms are classified as economically viable businesses if the income generated is sufficient to pay family labour at the average agricultural wage



and to also provide a 5% return on non-land assets. A farm that is not economically viable may be classified as sustainable if the farmer and/or the spouse have an off-farm income. Finally, farms that are neither economically viable nor sustainable are classified as economically vulnerable.

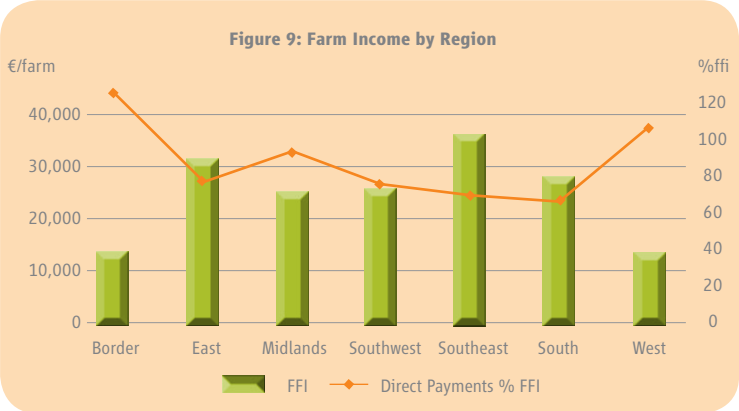
The proportion of economically viable farms decreased to 37% in 2012 (Figure 8) from 41% in 2011. Approximately 30% of farms are economically sustainable. Almost 33% of farms, or approximately 26,000 farms, are classified as economically vulnerable because the farm is not economically viable and neither the farmer nor spouse has off-farm income.



Tillage and Dairy farms are the most viable. The proportion of economically viable drystock farms remains low at, for instance, about 16% for Cattle Rearing farms.

**Regional Overview**

The average income per farm varies considerably by region. The Border region has the lowest average farm income at just over €14,000 per farm and the lowest income per hectare (Figure 9). The Border is also the most reliant on direct payments, contributing 122% of farm income. The average Single Farm Payment per hectare in the Border region is €294. The West region has the smallest farms on average and the lowest Single Farm Payments per hectare at €251. On average total direct payments comprise 107% of family farm income in the West.



The Southeast has the most profitable farms with an average farm income of just over €37,000 and income per hectare of €680, almost twice the income per hectare of the Border region. The Southeast has the highest Single Farm Payment per hectare at €369, but is the least reliant on direct payments as they contribute just 68% of farm income.

*Note: Please note that for comparative purposes information relating to years proceeding 2012 have been revised to account for methodological alterations in the 2012 National Farm Survey.*



Pictured at the AIB 'Future Prospects for Irish Agriculture' seminar held in the Silver Springs Hotel, Cork were Simon Coveney, Minister for Agriculture, Food and the Marine; John O'Doherty, AIB Regional Director for Cork; Denis O'Callaghan, Head of Branch Banking, AIB and Tadhg Buckley AIB Agri Advisor.



Pictured at the launch of the AIB/IFA Dairy Sector Report were (L to R) Kevin Kiersey, IFA National Dairy Chairman; Ken Burke, Head of Business Banking, AIB; John Bryan, IFA President and Pat Bogue, Broadmore Research.



## Irish agriculture over a working lifetime

**Matt Dempsey, Chief Executive, Irish Farmers Journal**

My older brother did architecture so, on a personal basis, I had to make a fundamental decision: would I learn about farming and agriculture or choose another career? Part of the decision was wrapped up with the desire to see the family farm stay in the family and ideally developed to where its potential could be realised.

On that basis, I applied to Warrenstown Agricultural College in Co Meath. It was full and they could not find another place so I applied to do Agricultural Science in UCD. There were roughly 100 in the class, 98 men and two women, both of whom married foresters which didn't do much good for the self esteem of the Ags but that's another day's work!

There are a lot of similarities between the climate surrounding agriculture in the late 1960s, early 1970s and today. EU, or Common Market membership was clearly on the horizon with the lifting of the French veto on British entry.

We have forgotten how the scales were tilted against Irish farming. Britain, by far our main market had a deficiency payment system on beef and lamb which was designed, especially on the beef side, to ensure that there was a ready supply of store cattle for further feeding and finishing on British farms. The Irish beef carcass trade was essentially dependent on the export of heavy Hereford type steers to the US forces in Germany and cow beef to Canada.

On the dairy side, a multi-tier price system was introduced to ensure that small scale producers stayed in business by paying them a higher price but the general rule was the higher the individual output the lower the price, except on liquid milk farms. Liquid milk was supplied into a tightly regulated market with Dublin and Cork both having their own district Milk Boards to regulate both the quantity, price and quality of milk – part of the reason being to ensure that consumers had a supply of milk during the winter months.

All of these restraints were swept aside in the run up to Common Market entry (other than the Milk Board system which lasted for another two decades). Dramatic price increases and hugely enhanced market access beckoned.

The five-year transition period to full EU price levels and market access was marked by two events. The first was the Arab boycott on oil exports and the subsequent quadrupling of oil prices in the 1973-'74 period. This coincided with a huge Russian purchase of US grain following a period of sustained economic growth in the western world.

The second factor was linked: this growth had stimulated an increase in cattle prices so that for a brief period in 1973, EU and world beef prices were the same and the external tariffs were removed on imports. This temporary distortion in the beef market, coupled with a wet summer and a build up of cattle stocks in anticipation of EU membership led to a catastrophic collapse in cattle prices in the autumn of 1974. While EU intervention provided some kind of floor for finished cattle, and may have benefitted meat processors at one end of the supply chain, producers of store cattle were forced to sell

onto a hugely over-supplied market and suffered very serious losses.

At that stage, Cork Marts owned the large IMP meat plants at Leixlip (now ironically the site of the Hewlett Packard plant and at Grand Canal Street in Dublin, now the site of smart blocks of apartments).

The industry did however recover quickly from the weather and price shocks and by the end of the transition period to EU membership, in his review published in 1980, Professor Seamus Sheehy had tabulated the prices for the main products in 1976/'77/'78 compared with 1969/'70/'71 as:

Cattle	+246%	Wheat	+220%
Milk	+260%	Barley	+206%

However, the oil price crisis of 1974 caused a surge in world inflation. In 1975, the inflation rate hit 25% but nevertheless the gains in income were very substantial with family farm income rising from €1,500 a year in 1972 to €4,500 a year in 1978.

Technically, it was an exciting period. My predecessor as Editor of the Irish Farmers Journal had chartered a jumbo jet to take a large group of dairy farmers to look at New Zealand dairy farming in 1972. Many of this group or their families are among the main dairy farmers in the country today.

Grassland management, new milking developments and an unlimited market for dairy products saw major expansion at farm level and the Friesian (mainly British type) becoming the dominant cow. It was also the period when the first rotary parlours went on to dairy farms.

On beef, the major winter housing needs were met by the development of slatted sheds which eliminated the need for straw – always expensive in Ireland. Slatted beef housing also allowed for the management of much larger numbers of cattle with mechanised feeding systems modelled on Continental and US lines being introduced.

It is hard to reconcile the situation back then with the emergence of the huge stultifying surplus that emerged in the 1980s. But when Ireland joined the Common Market in 1973, the community was only 75% self-sufficient in cereals and the Dutch pig industry in particular was expanding rapidly based on levy free imports of soya for protein and Manioc or Tapioca from the East Indies where they had learned its worth as an energy feed.

It was during the late 1970s and early 1980s that the new fungicide technology came on stream. Suddenly, Ireland which always had difficulty in producing predictable yields and quality of wheat became one of the world's highest producers per acre.

However, the surge in productivity was not confined to Ireland and there followed in the 1980s and 1990s a dreary succession of 'prudent price policy instruments' as well as a rigid quota system in dairying in 1984 and an ever tightening premium system that placed rigid limits on the number of cattle that would qualify for payment over and above the dramatically reduced beef and cereal guaranteed prices.

Suckler cows attracted their own historically based payments while on the tillage side, only land previously in tillage became eligible for the special support payments while the capacity to vary the land that could be compulsorily declared to be set aside acted as a valve to control supply and demand. While at institutional level, the policies centered on coping with ever growing world supply, the market place saw anaemic world demand, trade talks that looked for ever greater access to European markets and a growing divergence between European perceptions of food quality and those of overseas consumers. These differences in food quality perceptions were fuelled by a number of high profile cases – BSE, Foot and Mouth Disease and the Belgian Dioxin case. The resultant setting up of the highly credible Food Safety Authority has turned out to be a real advantage for the Irish food industry as it successfully allowed the transition from bulk commodity supplier to recognised high quality source of beef, dairy products, lamb, pig meat and poultry. In fact, baby food is now our single largest category of dairy exports.

Meanwhile at farm and industry level, life continued. The 70,000 dairy farmers that were in business has shrunk to about 18,000 today as scale and specialisation became ever more necessary, though the dairy processing industry has been much more lethargic, in recent years, in rationalising their own structures. The Dairy Board corporate structure continues to be clearly unsuitable for the new needs surrounding the sector, even though the necessity for the Body continues. Within the beef industry, we see the emergence of three very powerful family-owned groups with strong, international capacity.

We are coming to the end of yet another CAP reform process but the world demand/environment has changed beyond recognition with the emergence of huge new markets with a capacity to consume and an ability to pay. As ever, the agricultural environment is changing with the ebbs and flows of demand, supply and technology. Ireland is well placed to benefit with a grass base and products that are increasingly in demand. Suddenly it's more like 1972 than 2002!

## Managing the aftermath of drought in New Zealand

**Oliver Quigley, New Zealand dairy farmer, examines the challenges faced by farmers resulting from drought and outlines the supports that were made available to help farmers through this period.**

This summer saw the worst drought in New Zealand for the last 70 years. Beginning at the end of January initially it affected all of the North Island but from the end of March parts of the South Island were also declared a drought zone. The drought's impact varied across farming types because of differing supply and demand dynamics.

It is expected that the drought will cost the New Zealand economy NZ\$1.3bn (€780m) in export revenues. Farmers will have suffered additional costs and lost income of about NZ\$800m (€480m). Average incomes of North Island farmers are down by NZ\$100,000 (€60,000).

Lower interest rates and a vibrant economy cushioned the impact to the national exchequer of the drought in comparison to the last drought in 2007/2008. As the drought progressed and farmers started to run out of options many had to de-stock, selling stock that would normally have been kept on farm for longer and then by also selling capital stock (breeding ewes and cows). Dairy farmers moved to once a day milking after just 200 days into lactation and eventually dried off cows five weeks earlier than normal. Dairy farms will have to deal with reduced incomes and higher feed costs.

These decisions taken by farmers had a serious impact on cash flow as sales yards and slaughter facilities had three weeks waiting lists due to the volumes of stock that had to be traded. As a consequence there was a major drop in market prices in both the store and slaughter markets.

The Government and farm consultants held workshops and large field days advising farmers on how to cope with drought situations on a day-to-day farm management basis and to help with financial planning and budgeting. A series of publications, templates and drought management information booklets were also made available.

Setting feeding priorities and monitoring and initiating plans to ensure that farms recovered well when the weather broke and the drought ended was a priority for farmers in the affected regions. The focus of this phase was to ensure that next season's production would not be too badly affected by the drought and that the farm could again generate healthy cash flows.

### Engaging with the banks

Farmers were being advised to work with their accountants and farm advisers to identify the impact and the potential impact of the drought, both at that stage and over the coming year and talk to their banks about their needs.

This could range from initial relief on loan payments, overdraft extensions, restructured loans and/or additional lending in the longer term.

Many banks announced drought relief packages, with options including suspension of principal payments, emergency funding (sometimes at discounted rates), fee waivers, and giving special credit authorisation powers to their agri-business managers. Banks set up drought relief support providing emergency cash relief for additional feed, extra grazing and personal living costs.

The main agri finance institutions' posted advice on their websites, wrote to their farmer clients, and encouraged farmers through the farm media to carry out on going reviews of their budgets and to establish contingency plans as the drought progressed and feed conditions deteriorated. Agri lenders assessed farm businesses on the health of their resources - biophysical (land, pasture, crops, animals, infrastructure), economic (cash, assets, debt, tax, inventory) and human (farmer, farmer's family and staff).

The New Zealand Central Bank had previously flagged concerns about the



high level of indebtedness among farmers and its dairy concentration, and warned in its six-monthly financial stability report that the recent drought could “expose financial vulnerabilities across the sector”.

Parts of the agriculture sector in particular remain quite leveraged and progress in reducing debt loads in recent years has been not been very successful on many New Zealand farms. There is likely to be some increase in working capital borrowing from banks, in addition to recourse to Government support programmes as a result of the drought. Non-performing loans could rise amongst farmers who were already stretched to meet their commitments.

#### Industry collaboration

Federated Farmers ran a series of ‘Farming in Drought’ field days and organised shipments of feed from the South Island to the North and also sourced shipments of grain from Australia.

Fonterra announced in March that they would be increasing their milk solids payout and earlier advance payments on production supplied since July 2012. This meant an early cash flow of around NZ\$100,000 (€60,000) for the average farmer.

The Inland Revenue offered flexibility in the timing of tax payments and income assistance for farmers affected by the drought. Their offices set up an emergency help line from 8am-8pm weekdays and from 9am-1pm on Saturdays.

The Ministry of Health, in conjunction with local rural organisations, in the drought declared rural communities, held a series of workshops teaching people to recognise the signs of mental health problems and how to respond to having to manage on-farm issues caused by drought, financial constraints, ongoing uncertainty and stress. Other rural support trusts

continue to provide support for farmers on dealing with stress management, signs of depression and anxiety and more support groups for rural men have been created.

In the recent budget, the Government allocated NZ\$80m (€48m) towards irrigation projects as part of an estimated future exchequer investment of NZ\$400m (€240m) that will see potentially a further 420,000ha of land under irrigation. This should increase New Zealand exports by NZ\$4bn (€2.4bn) within the next five years.

#### Looking to the future

Now that some farmers are semi post drought but still face the winter with feed deficits, they are considering their options in drought prone areas and are investigating shade and shelter, soil-fertility, pasture species and the best animal genetics most suitable to their terrain and its challenges.

Further investment, if profitable, could lie in water harvesting or irrigation, specialty pasture species such as lucerne, chicory and plantain, planting of browse shrubs and fodder trees and the harvesting and feeding out of supplementary feed if margins allow.

It is widely mentioned by many agri commentators that the drought highlights the need for farmers to ensure that they financially position themselves for adverse events in the future as the reality is that these types of events are not uncommon.

Farmers needed to rethink the level of debt they hold to ensure it is manageable in the tough times and not just in the good times.

*[Figures in this article are in NZ dollars and have been converted to euro also. An exchange rate of \$1NZ : €.060 was used throughout.]*

## AIB/IFA Dairy Sector Report

AIB in partnership with the Irish Farmers Association recently launched a Dairy Sector Report which examines the outlook, opportunities and challenges for the Irish dairy industry. The report includes specially commissioned research undertaken by Amárach Research and Broadmore Research and includes both a farmer survey and expert interviews. This was the third in a series of SME sectoral reports undertaken by AIB examining key sectors within the Irish economy.

### Key Findings

#### Optimism

Farmers were more optimistic about dairy sector and their own business than about the overall economy.

- 52% believe that it will be at least 5 years before Ireland’s overall economic situation will improve; while,
- 57% believe that the situation will improve for themselves within 3 years.
- 50% of farmers intend to increase milk output between 2015 and 2020.

#### Opportunities in the next five years

- Abolition of milk quota was cited by 27% of farmers;
- Increased milk price was cited by 18% of farmers; and,
- Increased milk yield per cow was cited by 16% of farmers.

#### Challenges in the next five years

- 47% of farmers cited weather as the greatest challenge;
- 29% of farmers cited milk price volatility; while,
- The rising costs of inputs was cited by 20% of farmers.

#### Business Investment and Development

A significant proportion of farmers (65%), have invested in the their business in the past three years with further investment planned by 48% in the next three years.

- 52% of farmers do not plan to invest in their dairy business over the next three years;
- 30% of these farmers stated that they are happy as is and have no reason to expand.

#### Management Practices

In the next 12 months, 73% of farmers intend to improve their farming management practices as follows:

- 42% plan to improve grassland management;
- 19% plan to improve herd health status; and,
- 14% plan to improve financial management.

A copy of the AIB/IFA Dairy Sector Report is available on [www.aib.ie/outlook](http://www.aib.ie/outlook)



## Price volatility in farming

**Tadhg Buckley, Agri Advisor, AIB examines the impact of volatility and examines options available to farmers to reduce its effects.**

Volatility in both output and input prices has been a constant feature of Irish agriculture in recent years. In the past six years we have seen major fluctuations in the main output prices of beef, milk and in particular, grain and similar significant variations in input prices. Price volatility poses challenges for both farmers and industry as it makes financial planning and cash flow management much more difficult.

While price volatility has been much more pronounced over the past six years it is not a completely new phenomenon. Volatility on world markets has been evident for many years. However, farmers in the EU, were shielded from its worst effects due to market management mechanisms including quotas, intervention, export refunds and import tariffs. The bulk of these have now been removed or greatly reduced leaving EU farmers much more exposed to the volatility of world market prices.

### Why are farmers more exposed?

Farmers are price takers rather than price makers and are unable to pass on input price increases easily to their purchasers. As a result price volatility tends to have a more pronounced effect on primary producers (farmers) than secondary producers (e.g. dairy processors, grain merchants) who can somewhat more easily pass on input price increases. It should be noted though that the increased power of retailers has made it much more difficult for processors to pass on raw material and other input price increases. Generally they can only do so, in whole or in part after a considerable time lag. In addition, Irish farming is heavily export-dependent and this, together with the seasonal nature of much of our mainly commodity production makes Irish farmers more exposed to price volatility than their EU counterparts.

### Which farmers are most exposed?

Farmers with a high cost of production are much more exposed to significant price variations than low cost producers. During periods of high output prices, the vast majority of producers are profitable; however during periods of low output prices those with a high cost of production are much more heavily effected financially than their low-cost counterparts. It generally takes high-cost producers much longer to recover from a depressed price period, and in many cases the losses incurred may take years rather than months to overcome.

### How to reduce the effects of price volatility

The options available to Irish farmers to manage price risk are limited. Some of the options available include:

- Improve competitiveness – this is a very effective way of positioning your farm business to deal effectively with price volatility as it reduces the financial impact of low output price periods;
- Build a cash reserve during high margin periods – this reserve can then be used to fund any deficits incurred during times of low output price;
- Use bank finance to fund cash deficit periods – the benefit of this option will depend on the efficiency of the farm business. For high-cost

inefficient producers there may be substantial deficits to finance and it may take a long time to repay the deficit incurred, possibly not before another low-price period occurs;

- Forward purchase inputs and adjusting capital spending (carrying out farm improvements during good times and postponing them during bad times) – these are methods of managing cash flow in order to prepare the business better for a downturn; and,
- Income averaging – this can be used in order to reduce variances in annual tax liability which can allow for better cash flow management.

### Managing price volatility – other potential options

There are other options which have been adopted in other countries to help farmers manage price volatility. These include:

1) *An income stabilisation tool*: this is a subsidised fund to which farmers would contribute under a specific set of circumstances. An income stabilisation tool proposal is currently an option as part of the Pillar II CAP Reform proposals. Under this proposal farmers would be able to access the fund under a particular set of circumstances.

It is likely that there would be a high level of administration associated with a fund of this type and it remains to be seen whether Ireland would have an interest in putting such a scheme into operation.

2) *Hedging using futures or forward contracts*: this method is widely used in the US and is now available in Ireland through grain forward contracts and fixed milk price schemes. They offer the advantage of stability and allow farmers to plan forward. The disadvantage is that you are tied in for the duration of the contract to one supplier.

3) *A farm savings accounts*: this is a designated deposit account designed to encourage farmers to build a cash fund during high margin periods in preparation for low-margin periods. Its use is normally encouraged through the incentive of tax deferral. Variants of such accounts are used in Canada and Australia among other countries. They are similar to income averaging from a tax point of view but they also encourage farmers to build up a cash reserve.

### Conclusion

Price volatility and its effects has become much more pronounced over the past six years due to the reduced level of intervention by the EU in market management. All indications are that this level of volatility is likely to continue into the future. Improving efficiencies is one of the best methods of positioning your farm business to cope with volatility. There are also other options currently available including income averaging and the use of forward contracts. Internationally, there are other options which could be adopted in Ireland to give further assistance to farmers. Whatever options are taken it is vital that Irish farmers position themselves well for continued volatility into the future.