

AgriMatters

AIB supporting the Irish Agricultural Industry



Autumn 2009



Tullamore Show & AIB National Livestock Show 2009

In This Issue: Cashflow Management / The Dairy Market

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Welcome to the Autumn edition of Agri Matters

Michael Dowling, Head of Agri Strategy, AIB

Welcome to the Autumn edition of Agri Matters. As usual, we are producing this edition to coincide with the National Ploughing Championships, the major agri event of the year.

By any standards, this has been a very difficult farming year. Extremely low prices for some commodities – in one case as low as in the mid-1980s – have been compounded by weather conditions as bad as anything experienced in living memory, and all of this in the midst of a severe economic recession. In one way or another, articles in this edition reflect this very challenging background. In particular:

- the agri review analyses the current situation and looks forward to what is to come
- the section on the dairy market describes the huge volatility that has taken place within the past two years
- John Bergin's article outlines the current grain market and describes some risk management possibilities for farmers
- Pat Butterly's contribution describes the current agri banking scene and offers advice to farmers who may be experiencing short-term difficulties
- we have an article on cash flow planning, including a template of a cash flow planner that may be of practical use to some farmers
- there is our usual piece on the current economic scene and outlook.

Finally, we have included a short summary of the recently published report from Teagasc on its National Farm Survey for 2008, which analyses in detail the farm income situation in that year.

We have tried to put the current situation into a multi-annual context and to look forward to what the future may have in store. The industry has dealt successfully with low prices and difficult markets in the past. It has survived in difficult general economic circumstances. Accordingly, this edition reflects a challenging, but not a hopeless, situation. And, as we go to press there are increasing signs that the international economic situation has turned the corner and furthermore that agricultural commodity markets are beginning to recover. It looks as if 2010 will be a distinct improvement on this year.

More immediately all of us are, as usual, looking forward eagerly to the 'Ploughing'. Despite the difficult background, we expect it to be again a wonderful event. We wish every success to the organisers, competitors and exhibitors, and hope that all who attend find it enjoyable and instructive. Above all, in this soggy year, we pray that the clerk of the weather will relent and let us have an Indian summer, at least for a few days in the fourth week of September.

Michael Dowling
Head of Agri Strategy

AIB and European Investment Bank – Funding for SMEs (including farmers)

Following discussions between AIB and the European Investment Bank (EIB), a five year €100 million loan fund for investment projects for Small and Medium Enterprises (SMEs), including farmers, has been agreed between the two institutions. This EIB funding allows the Bank to enhance our competitive range of lending options for our SME and agri customers.

The EIB loan can be used to finance investments that are incurred in the development of an SME. Examples include:

- The purchase of tangible assets OTHER than land (including farmland)
- Purchase of new plant and/or machinery
- Development, planning and financing costs during a construction phase of a business premises.

Full details are available from your local AIB branch.

Lending criteria, terms and conditions apply. Credit facilities are subject to repayment capacity and financial status and are not available to persons under 18 years of age. Allied Irish Banks, p.l.c. is regulated by the Financial Regulator.

Our Agri Adviser Team



PATRICK BUTTERLY
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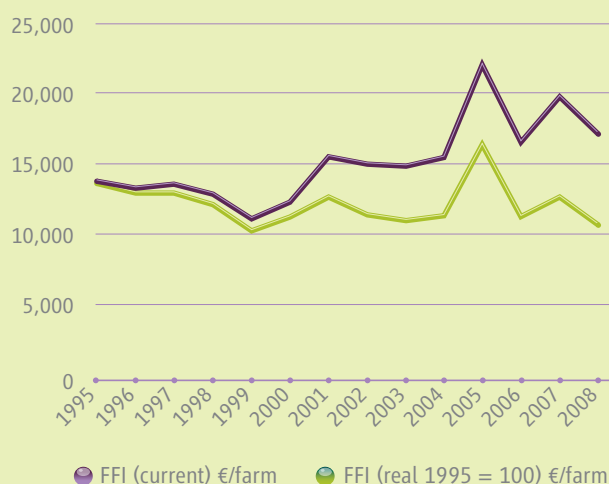
TADHG BUCKLEY
AIB MALLOW

National Farm Survey 2008

Since our last edition, Teagasc has issued its report on the 2008 National Farm Survey. The overall outcome – an average 14% drop in family farm incomes compared to 2007 – was not a surprise, as a substantial drop in farm incomes had been signalled in earlier CSO estimates. While farm incomes have fluctuated over the past decade and a half, in real terms the trend has been generally downwards (see Figure 1).

As usual, however, the results of the national survey provided a wealth of detailed information on the make up and distribution of family farm income.

Figure 1: Family Farm Income (FFI) Per Farm 1995 – 2008



Source: National Farm Survey 2008

The income decrease was most pronounced in the case of large scale producers, tillage farmers and farmers in mixed dairying systems. Income in the cattle sectors was generally up. The drop in income is mostly accounted for by the exceptional increase in input costs but, in the case of tillage, there was also a significant fall in the value of gross output (down 11% on average).

Off farm income

The percentage of farms in receipt of some form of off-farm income at 79% was similar to earlier years. The percentage of farms where either the farmer or spouse had an off-farm job varied from 52% on specialist dairy farms to 63% on cattle rearing and tillage farms. Again these figures were broadly in line with the previous two years but they are up about 8% since 2002.

Income per hectare

In terms of income per hectare, dairying was, as usual, very much ahead of the other sectors and, in fact, gave a return which was more than double the average of all sectors (this sectoral gap is likely to be very much narrowed this year). As is clear from Table 1, with one exception, the relationship in terms of income per hectare between the sectors was relatively similar in the case of both full-time and part-time farmers. The exception was the tillage sector, where part-time farmers fared relatively better than their full-time colleagues and indeed in absolute terms the return per hectare on part-time tillage farms was substantially higher than on full-time ones.

Direct Payments

The figures once again underline the critical importance of direct payments in both the value of gross output and family farm income. They show that the ratio of these payments to gross output at 31% (the CSO figures on

Table 1: Income per ha (€/ha)

	All systems	Dairy	Mixed dairy	Cattle rearing	Other cattle	Sheep	Tillage
All farms	463	961	507	260	361	281	335
Full-time	605	980	555	342	446	309	300
Part-time	302	577	329	234	326	259	427

Source: National Farm Survey 2008

aggregate farm income put this ratio at 25%) was unchanged in 2008 compared to 2007, but that last year direct payments accounted for 103% of family farm income compared to 84% in 2007. Direct payments are important (i) in all farm systems, varying from 45% of income on dairy farms to 180% on cattle farms; (ii) on all farm sizes, varying from 180% on smaller farms to 80% to 90% on larger ones, and (iii) in all regions, varying from 80% in Cork and Kerry to 180% in the border counties. Table 2, based on the National Farm Survey results, gives a sectoral breakdown of average direct payments paid in 2008.

Table 2: Breakdown of Direct Payments in 2008 (€)

	All systems	Dairy	Mixed dairy	Cattle rearing	Other cattle	Sheep	Tillage
All Direct Payments	17178	20438	21772	13516	16069	15492	25242
Of which:							
SFP	11854	15472	16269	8044	11258	8447	21209
REPS	2857	2219	3163	2658	2604	3877	3427
DCAS (i)	1989	1967	1985	2242	1832	2712	339

(i) = Disadvantaged Areas Compensatory Allowances

Source: National Farm Survey 2008

From Table 2 above, it is clear that the Single Farm Payment (SFP) is by far the most important direct payment. In the sheep sector the SFP accounts for 55% of total direct payments. In all other sectors it accounts for 70% or more. The predominance of the SFP is evident not just in terms of farming system but also in terms of farm size, full-time or part-time farming, and regionally. Even in the border counties and Connacht, where REPS and the DCAS are of relatively greater importance, the SFP accounts for between 55% and 60% of total payments. This underlines the critical importance of the negotiations to take place over the next couple of years on the post 2013 CAP, which will centre very much on the future of the SFP.

On-farm investment

The Report's figures on gross new investment and loan balances are of particular interest. Teagasc estimate that gross on-farm investment on Irish farms in 2008 was €2 billion (up from €1.4 billion in 2007) and that investment totalled €4.5 billion in the 2006 – 2008 period. Average new investment per farm was €19,480 which was a 59% increase on 2007. By far the biggest investments were on large scale dairy farms, and these farms also had the biggest increase in closing loan balances. The second and third biggest investments were on large scale mixed dairy and tillage farms. Investment-led borrowings increased by 30% and 40% on full-time farms. Loan balances increased by 60%, 70% and 80% on full-time dairy, suckler and sheep farms respectively.

This unprecedented level of investment on Irish farms has, to a large extent, been driven by the Farm Waste Management Scheme. Teagasc comment that repayment of capital and interest will affect family farm income into the future. The phased payment of the farm waste management grants should reduce this burden.

Reflections on a difficult year

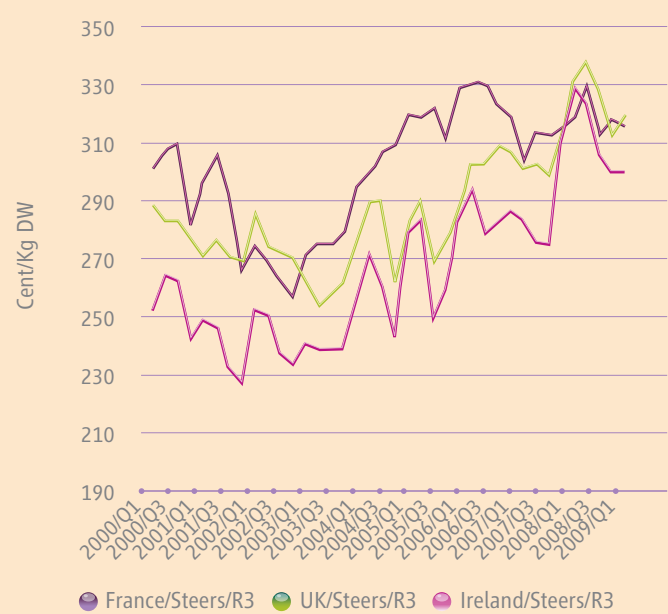
Michael Dowling, Head of Agri Strategy, reflects on the year so far and the difficulties 2009 has posed for all those working in the agri sector.

Coming into 2009 we expected it to be a difficult year and, in the event, it has turned out to be, if anything, somewhat worse than anticipated. The only significantly positive element has been the drop in input costs – admittedly from a high plateau. Depressed market prices, combined with adverse weather conditions and the effect of the general economic recession, have made this a stressful year for farmers in most sectors. 2008 was a year in which the benefit of reasonably good prices was nullified by an extraordinary rise in input costs. This year has seen the opposite phenomenon of the benefits of sharply reduced input costs being counteracted by lower prices. There are, however, some indications that the price situation is beginning to improve.

Beef: Average prices for the year are likely to be approximately 7.5% down on the relatively strong 2008 price levels. When the strong trade in live exports is taken into account, output is expected to be close to last year's levels. There are signs as this is being written (late August) that prices are beginning to improve in response to tighter supplies. Looking at a longer timeframe, beef prices in this decade peaked in the late summer of 2008 and have been declining since. There was no noticeable spring bounce this year. Nevertheless, average prices this year will still be above the levels of the first eight years of the decade. For brief periods in 2005, 2006 and 2008 Irish prices were on a par with British prices and, at peak in 2008, they exceeded French prices. Since then, the traditional gaps between the relative price levels have re-opened but not to anything like the same extent as in the early years of the decade (see Figure 1).

Pigmeat: Prices are, on average, likely to be 4.5% down on 2008 but still the third highest this decade (see Figure 2). Throughput has been very gradually falling throughout the decade (and is evident in Figure 3). As a result of the cull caused by the dioxin problem at the end of last year, the drop this year will exceptionally be about 7.5%. Output will, however, recover in future years.

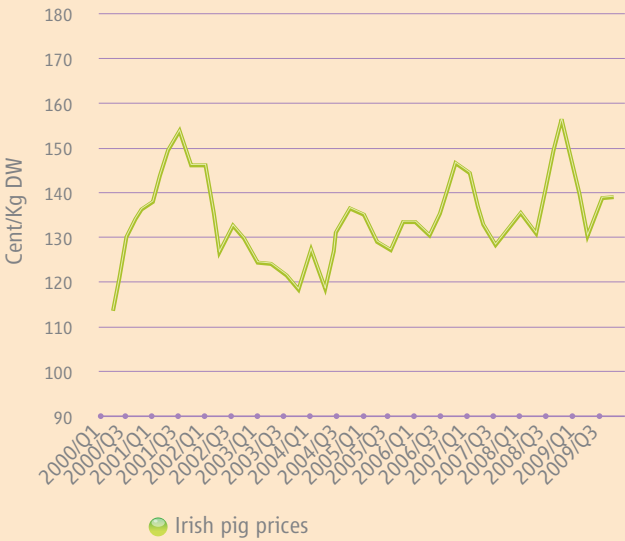
Figure 1: Cattle Prices



Source: Bord Bia

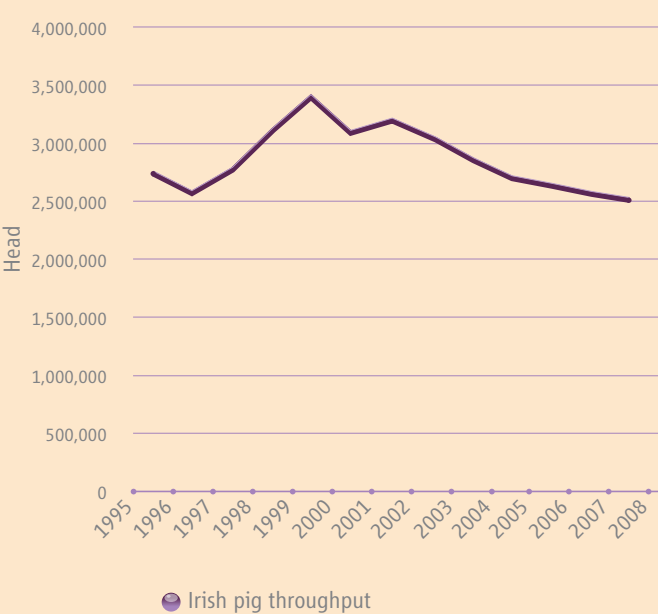
Lamb: Prices declined gradually in the first half of the decade and have been slowly rising since. This year is likely on average to see a marginal improvement on 2008. In line with the trend in recent years, output is, however, likely to be 4% to 5% down. Throughput has declined in every year since 2005 and is now 25% lower than in that year.

Figure 2: Pig Prices



Source: Bord Bia

Figure 3: Pig Throughput at Export Meat Plants



Source: Bord Bia

Reflections on a difficult year *continued*

"The sharp drop in prices has severely affected the profitability of milk production"

Milk: With the carryover into the early months of 2008 of the exceptionally high milk prices from the previous autumn, the average price last year of about 33c/l was similar to the 2007 price. The deterioration in international and European dairy commodity prices, which began in the second half of last year, has, however, continued into, and intensified in, 2009. As a result, prices this year are not likely to average more than 22c/l. The sharp drop in prices has severely affected the profitability of milk production and, as a result, the availability of additional milk quota this year will not lead to any increased production either in Ireland or in Europe generally.

There is tentative evidence that prices are beginning to recover, but it is likely to be well into next year before the recovery will be in anyway pronounced. The longer term outlook for the dairy sector, however, remains positive, as global economic recovery should see a sustained improvement in demand, particularly in the developing world. The situation on the dairy market is treated in more detail in the article on the Dairy Market (see page 11).

Cereals: We indicated in our Spring/Summer edition that, at that stage (April), the outlook for the grain harvest was reasonably promising. That scenario has changed dramatically in the meantime. Better than expected harvests in the US and Europe, together with uncertainty about demand in a depressed economy, have pushed prices well below the levels confidently expected only a couple of months ago. In Ireland, for instance, prices for barley may not be above €90 per tonne, compared to about €130 last year (and over €180 in the peak year of 2007). If that picture remains unchanged, it would mean that prices had fallen back to 2005 levels. Ireland is, of course, not unique in this situation. In early August grain prices in Europe and the US were 25% to 30% below 2008 levels. While this situation may not change significantly as the year goes on, lower plantings in response to this year's drop in prices, and an improving agricultural economy, should see an improved tone to the market next year.

Input costs: There has been a substantial reduction in input costs this year. Feed prices are down by between 7.5% and 15%, fertiliser prices by up to 25% and energy by more than 20%. With the exception of soya, prices of the main feed ingredients are likely to remain relatively low in the short to medium term and oil prices are at 2006 levels and well below the prices that were obtained in the middle of last year.

The drop in input costs is, of course, having a beneficial effect on farm incomes, which, as always, will be underpinned by the high level of direct payments. This combination will not, however, be enough to offset the effect of the drop in market prices. As a result incomes are likely to fall by over 10% this year.



Pictured at the launch of the 2009 AIB/Macra na Feirme Club of the Year Competition are Anne Finnegan, Agri Strategist AIB, Michael Gowing, National President Macra na Feirme and the finalists of the Blue Jeans Country Queen competition.

Managing your cashflow

Volatile prices and yields mean that farmers are often faced with cashflow uncertainty. Depressed commodity prices, delayed FWMS grants and REPS payments, capital investment carried out from cashflow and adverse weather conditions have all combined to negatively impact on the cashflow situation on Irish farms this year. Managing the cash inflows and the cash outflows of the farm is one of the most important aspects of the farm business, but unfortunately it often does not get the attention it requires. Cashflow is the lifeblood of any business and farming is no different. In an ideal world cashflow would be predictable, but in reality and especially in farming it rarely is. The careful management of the farms cashflow is therefore critical to its survival.

What is cashflow planning?

Cashflow planning involves assessing when cash is likely to come into and move out of your business. It involves planning ahead so as to ensure you have sufficient working capital, to meet the needs of the farm business when required. It is an important tool on farms to ensure there is sufficient cash available to meet farm costs, family living expenses and loan repayments as they fall due.

Benefits of cashflow planning

Cashflow planning allows for better management of the farm finances by helping to identify periods of cash surplus and deficit. It therefore allows you to take the necessary corrective action to deal with any cashflow deficits, while also allowing you to take advantage of opportunities that may arise from cash surpluses.

A cashflow statement will outline to you what your working capital situation is like at present, and likely to be in the short term. If you feel you will need additional working capital at some stage during the year, approaching your bank early before a cashflow problem emerges will make finding the best possible solution for you and your farm business easier.

If you approach your bank with a new funding proposal, a cashflow statement together with cashflow forecasts for the coming year will enhance your proposal by portraying your understanding of your business. It will provide you with better knowledge of your farm finances and this will allow you to structure your loan repayments to suit your farm needs.

How to begin

It is good practice to begin each accounting year with a projected cashflow statement for the coming year, outlining what you think the cash inflows and outflows will be during the year. It is not too late to produce your cashflow statement for the remainder of the year.

We have produced a simple cashflow planner template which can be used to produce a cashflow statement for the year. We recommend that you use the template to plan your cash inflows and outflows for the remainder of the year if you have not already got a cashflow plan in place. This will allow you to get to grips with the cashflow requirements of your farm for the remainder of the year and plan accordingly.

At the beginning of the year it will be difficult to plan for all the cash inflows and outflows that will occur during the year and when they are likely to occur. As such, the initial compilation of a cashflow statement will require some effort in examining farm records. Looking back on the previous year will however provide a good template for planning the year ahead.

Start by examining the income receipts from the previous year. Milk and livestock sales should be easily attributed to an individual month by examining creamery and mart/factory receipts. You should take note of the numbers of cows that were milked and the stock numbers sold. You can then use this information to help predict your cash inflows for the coming year. If you are expanding herd size you may have less stock to sell this year. Prices will undoubtedly change from last year and the weather may impact on sales/production. However, include a price and allocate the cash inflow to a specific month. The SFP will arrive between October and December

and include any other payments you expect to receive throughout the year including REPS. Your bank statements will also provide you with a good record of any additional payments/receipts you received during the previous year which are likely to be received again.

When you have examined your income receipts it is then time to take a look at expenditure and all the relevant cash outflows from the farm. Again bank statements accompanied by cheque books will be a good source of information. Examine each individual cheque and try to attribute the correct cost to the relevant areas in your cashflow statement. Your merchant/co-op bill can be used to help with this process. You should also examine all invoices and receipts as they may have been paid for in cash. Again, looking back over last years' expenditure is a good start for trying to predict the year ahead. If there are specific times each year that you pay your contractor or your merchant/co-op, include them in the cashflow statement together with an estimate of the cost. Remember these can be easily adjusted to take account of changing circumstances as the year progresses. The important thing is to include them in the plan and amend if necessary.

As the year progresses you should record the cash inflows and outflows as they actually occur in the cashflow statement. A comparison of the projected and actual cashflow will enable you to see if things are going according to plan and if not, to formulate solutions for unanticipated problems or take advantage of favourable circumstances. It is important that at the end of each year you complete your cashflow statement, review the document and make use of the information contained in it.

Your first cashflow statement will probably be the most difficult to prepare and the least accurate. It may be beneficial to enlist the help of a professional with your first cashflow statement as predicting cash inflows and outflows can be challenging. Remember the success of your cashflow analysis and benefit of your cashflow statement will depend on the accuracy of the information used. The process of cashflow planning will get easier, the information produced should get more accurate and the benefits should be greater in each subsequent year.

Information a bank may require from you when assessing a loan application

- A farm business plan including details of farm finance required, its purpose and proposed repayment schedule. Ideally the plan would include income and expenditure projections and cashflow budgets.
- Up-to-date financial accounts for two to three years.
- A farm profile including details of land farmed, production system, livestock, farm machinery and existing financial commitments.
- There may be other information required by the bank if some of your accounts are contained with another financial institution such as up-to-date bank statements.

Cashflow Planner												
Year:	January	February	March	April	May	June	July	August	September	October	November	December
Receipts												
Single Farm Payment												
Milk sales												
Livestock sales												
REPS												
Forestry Premium												
Salary												
Grant Bridging Loan												
Term Loan top up												
Grant												
Other:												
Other:												
A. Total Receipts												
Expenditure - Farm												
Fertiliser, seed, spray												
Purchased feedstuff												
Livestock purchases												
Veterinary, Medicine & AI												
Contractor charges												
Building farm repairs & maintenance												
Machinery operation & maintenance expenses												
Upkeep of land												
Transport												
Casual labour/wages												
Rent												
Insurance												
Bank loan repayments												
Professional fees												
Motor expenses												
Quota leasing												
Living expenses												
Other:												
Other:												
B. Farm Expenditure Total												
A - B Cashflow Surplus/Deficit												
Opening Cash balance (Start month)												
Closing Cash Balance												

Approaching your bank

We in AIB understand that it has been a difficult year for farmers and we know that some people are experiencing financial difficulties. If you are experiencing financial pressure, the important thing is not to ignore it. Address the situation and get help as early as possible. It is important to make early contact with your local branch. It is advisable to arrive early and arrive prepared - this will allow your bank to work with you in an attempt to minimise the financial impact on your farm business and household.

If you are at present experiencing cashflow difficulty, you will need to firstly identify the cause of the problem. Explain the problem to your Relationship Manager, establish how much money you will need to get through the next 12 months and discuss the options that are available to you. Where they can, your bank will try to work with you to find a solution.

Dates for your diary

Oct 15-16: Teagasc Forage Legume Conference, Cork

Nov 5: Teagasc Agri-environment and REPS Conference, Ballinasloe

Nov 10: Teagasc National Pig Farmers Conference, Cavan

Nov 11: Teagasc National Pig Farmers Conference, Clonmel

Nov 18: Teagasc National Dairy Conference, Mullingar

Nov 19: Teagasc National Dairy Conference, Killarney

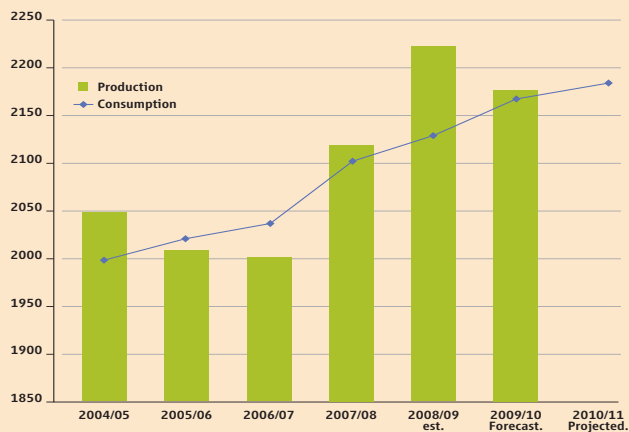


Going with the Grain

John Bergin, Grain Trader, R&H Hall examines the current global grain supply and demand dynamics and explains how the Grain Futures Markets work and the implications for Irish producers.

The global grains supply and demand picture has transformed completely in the past two years from one of absolute shortage with historically low stocks to one today of massive oversupply.

Figure 1: Global Grain (Wheat, Rice & Course Grains)



This change from supply shortage to massive overhang has seen wheat prices trade from almost €300 per tonne at their peak to under €100 per tonne today. The old adage ‘nothing cures high prices like high prices’ was never more appropriate. Following the high prices of 2007, farmers across the world increased plantings dramatically adding 6 million hectares to the total global wheat area planted alone. This, combined with massive yields, resulted in the biggest grain crop on record in 2008/09 at over 2.2 billion tonnes.

This, coupled with reduced consumption due to the global recession, saw a global stocks recovery. Negative developments from a price and planting perspective, of numerous other variables (funds, currency, access to finance etc) and the aforementioned abundance of wheat on the world market, give an indicative picture of producer planting intentions going into the 2009/10 crop year.

With this in mind, we headed into the current campaign saying plantings will be back, yields can’t be as good and consumption will be better than forecast, resulting in higher prices. What has actually happened of course has been quite different. For simplicity, we will just look at wheat in this example. Whilst both plantings and yields are back somewhat (see Table 1), in some countries such as the power houses of France and Germany, yields are actually better than last year. Whilst production is lower than last year, it is more than adequate to meet current world demand when combined with the healthy stocks from last year’s record harvest – this is the core issue.

Table 1: Wheat Production in Selected EU Countries

	Area (million ha)			Yield (tn/ha)			Production (million tn)		
	2007	2008	2009	2007	2008	2009	2007	2008	2009
Germany	2.98	3.21	3.24	6.97	8.09	8.16	20.77	25.97	26.44
Denmark	0.69	0.64	0.73	6.56	7.89	7.72	4.53	5.05	5.64
Spain	1.33	1.54	1.23	3.84	3.62	2.74	5.11	5.57	3.37
France	4.78	5.06	4.9	6.44	7.29	7.61	30.78	36.89	37.29
UK	1.83	2.08	1.88	7.22	8.28	7.79	13.21	17.22	14.65
Poland	2.11	2.28	2.22	3.94	4.07	4.05	8.31	9.28	8.99

Figure 2: Global Wheat – Stock:Usage Ratio

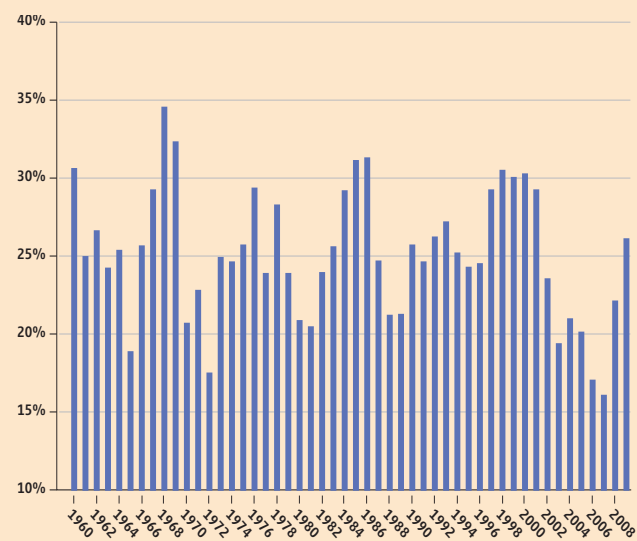
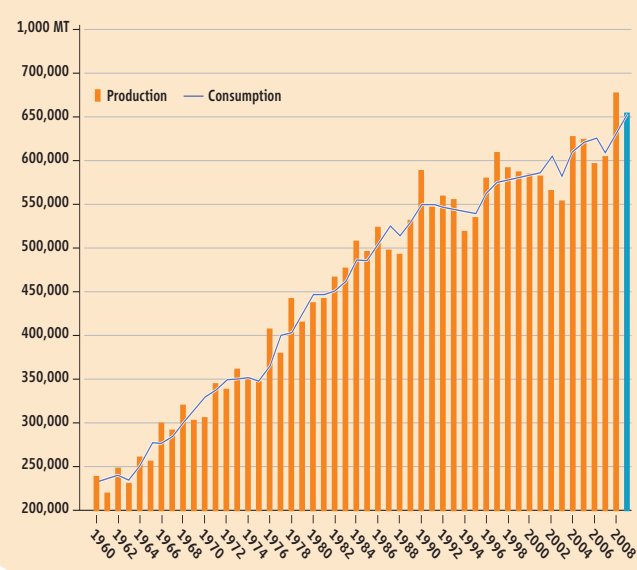


Figure 2 shows the increase in stocks-to-usage ratio for wheat from the very low 16% in 2007, to a now extremely comfortable 27-28% in 2009. Global wheat stocks are considered safe at approximately 150 million tonnes and are currently at 170 million tonnes and forecast to rise to 184 million tonnes in 2009/10.

The chart below (Figure 3) clearly shows the overhang of wheat on the market created by last year’s increased plantings and yields leading to the continued drift in prices. For the short-to-medium term the global grain market must deal with the overhang of stocks in the market and trade at the price level that will find demand.

Figure 3: Global Wheat Production



Grain Futures Markets Explained

Grain Futures Markets are International Exchanges enabling institutions and businesses to manage their price risks. On their trading floors and systems, buyers and sellers meet to trade futures and options contracts. A range of products are traded such as commodities, foreign currencies, interest rates and stocks.

A Futures Contract is a legally binding commitment to deliver, or, take delivery of, a given quantity and quality of a commodity at a price agreed upon, at the exchange, at the time the contract is executed. In practice over 95% of all contracts traded are closed out and not taken to delivery. Members of the exchange include the world's largest banks and investment houses as well as independent traders (Merchants, Co-ops, etc) and brokers.

The Futures Markets are highly regulated through a financial safeguard and clearing system unique to Futures Markets: the exchange clearing house guarantees each and every trade made on the exchange by acting as counterparty to all trades.

To make this process work, each futures contract is based on a clearly defined set of specifications on quality, time and place of delivery leaving price as the only variable to be determined at the time of trading.

Grain growers are operating in a highly volatile international market and need to find a means to reduce risk and its financial impact. Figure 4 shows the price movement and volatility on the Nov '09 Matif Wheat contract over its lifetime.

Figure 4: Nov '09 Matif Milling Wheat (Apr '08 – Aug '09)



Benefits of Futures Markets

- **Managing Price Risk** - where growers are exposed to prices falling and processors are exposed to prices rising, futures markets can help to manage this risk for both parties
- **Complete Price Transparency** - the price is traded each working day and available for all market players to see
- **Security** - due to regulations in place as outlined above
- **Anonymity** - when trades take place the buyers and sellers are unknown to each other
- **Liquidity** - you can buy or sell on any business day and it is easy to get in or out of a contract.

You are required to deposit around 10% of contract price (currently €12/tonne on Matif Wheat), you can buy or sell and you are subject to Margin calls based on Market movements against you.

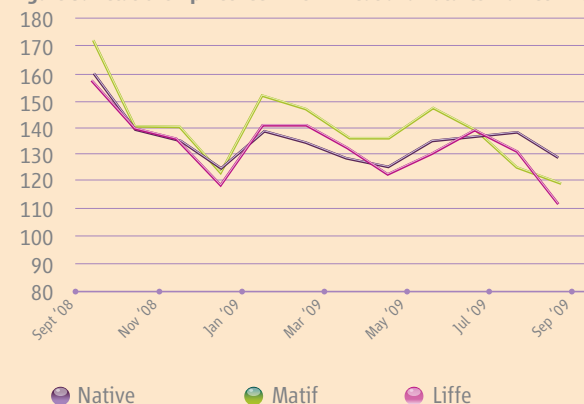
Factors affecting the price

- Supply and demand and the markets view as to whether it is in over or under supply
- Currency movements and their impact on international prices
- Funds and their view of the market and indeed the world economy. These players move in and out of the market often completely ignoring market fundamentals and for a completely different set of reasons to physical traders (momentum, trends)
- Oil and other commodity prices and the general feeling towards them
- Weather conditions, crop progress, along with future planting intentions.

Markets relevant to Ireland

The biggest exchange in the world is the Chicago Board of Trade (CBOT) and this exchange is the global trend setter for corn, soya and wheat prices. The European exchange is called Liffe. Traded on this exchange are Feed Wheat in pounds (£) and Milling Wheat, Corn, and Oilseed Rape in euro (€). In general the LIFFE exchange sets the daily, weekly and forward prices traded in Ireland up to a 32-month period for the relationship between Irish Wheat and Futures Market prices.

Figure 5: Relationship Between Irish Wheat and Futures Market Prices



Barley is not traded to any large degree on Futures Markets and, as such, is much more of a physical market but, in some cases, feed wheat markets can be used to create somewhat of a hedge. If not perfect, it is certainly better than doing nothing.

Wheat is the largest traded cereal globally. As we have demonstrated above, Irish prices follow international markets, although not always at the same speed. However, physical or cash markets tend to react more slowly as it is the Futures Markets themselves which create the physical price. While it is probably not practical for Irish growers to take part directly in Futures Markets, it is very easy for them to follow movements and price trends and, as such, sell grain forward via their Merchant or Co-op.

Irish grain growers must know their cost of production as there is no point in tackling your price risk exposure without knowing what costs you need to cover. Set a minimum price target, identify the price level at which you are prepared to sell and you should sell a percentage of your crop when this level is reached. The price level you target should be based upon your costs of production, risk profile and market view. Stick by your decision and sell when the market reaches your first target.

Understand and monitor the market so as to take advantage of price shifts in your favour and find a partner to act on your behalf. Try to recognise the market drivers, act on them and utilise all the information available to you. Develop a strategy that works for you – you will need a plan which takes into account your minimum acceptance price, as well as cash flow and business considerations. Once you have sold, you can't change what you have done or sell twice and there is no point in beating yourself up if the market price rises. Be fully aware that numerous outside factors will have an impact on grain prices and be alert to these factors.

Will the Irish grain grower be protected from the huge volatility of the market?

The answer is probably no, but it should help to protect him/her from the extremes of the market place and help to get him/her off the really dramatic roller coaster and on to a more gentle one.

So, is there any hope for Irish grain growers? Yes, but more in the long-term. Hope stems from plantings, which could be down 10% globally this year due to current prices, which are below the costs of production. We are unlikely to get a third year of high yields and ideal growing conditions. Hope of a global economic recovery and continued population growth are factors that give us some optimism for a recovery in prices. One thing is for certain - we will see continued wild volatility and big price movements in grain markets for the next few years, but the underlying fundamentals suggest grain prices should recover in the long-term.

Economic outlook

The Irish economy remains in the grips of a deep recession, driven in large part by a very sharp decline in housing activity. However, in addition to this marked fall off in housing output, the economy is also grappling with other significant headwinds, including the marked slowdown in the global economy, a higher exchange rate, ongoing problems in the financial sector (which has resulted in tightened credit conditions), rising unemployment, weakening confidence and fiscal tightening. Thus, after a contraction of 3.0% last year, GDP growth is forecast to fall by as much as 9.0% this year.

Conditions are set to remain difficult into 2010, when GDP is forecast to contract by another 3.0%. The economy is then expected to recover from 2011 onwards as the global economy swings upwards and the impact of the sharp adjustment in the housing sector wanes. Economic data from the major economies are already showing that the global economy appears to be over the worst of the recession, with demand conditions set to improve further over the forecast period.

While the economy is going through a very turbulent period at the moment, the medium-term growth prospects for the economy remain very favourable, judging by demographic trends. Ireland has the youngest population in the EU and the EU authorities expect the Irish population to rise by 22% by 2020. Thus, some commentators, including the ESRI, believe that the economy continues to have the potential to grow by an average 4% or more out over the medium term.

For now, however, the downturn in the economy is having a severe, negative impact on the public finances, which have deteriorated rapidly after more than a decade of budget surpluses. The general Government budget balance moved from a small surplus in 2007 to a deficit of 6.3% of GDP in 2008. Even after taking severe correction action, the Government currently anticipates a very large budget deficit of 10.75% of GDP for 2009. In addition to the tough measures already announced, the Government has indicated that further corrective fiscal measures will be introduced over the next four years to reduce the budget deficit to 3% of GDP by 2013.

The slowdown in economic activity is also having severe consequences for the labour market. The unemployment rate has been moving upwards for well over a year now, though data over recent months indicate that the rate of deterioration in labour market conditions is at least easing. Nonetheless, the unemployment rate had still climbed to 12.4% by August 2009, up

from 4.5% in late 2007. It looks set to rise to 15% over the next couple of years. Ireland has not been unique in terms of this rapid slowdown in the pace of growth, with the contraction in the eurozone as a whole, as well as the ongoing problems in credit markets and falling inflationary pressures, leading to official interest rates being cut to historically low levels of 1% in May. With a view to improving liquidity the European Central Bank has also injected substantial funds into money markets, while also commencing an asset purchase scheme. Rates are expected to remain at very low levels for a prolonged period of time, certainly well into 2010.

Irish inflation has been on a sharp downward trend for some months now and by July of this year the annual CPI rate had fallen to -5.9% compared to a rate of 4.4% for the same period last year. Given the scale of the downturn in the pace of economic activity, as well as falling interest rates and the trend in international commodity prices, easing price pressures are expected to be a feature for some time yet, which is good news from a competitiveness point of view. The CPI is forecast to decline by an average of over 4.0% for 2009 as a whole, before rising modestly in 2010.

Economic Forecast – Ireland				
(Annual % Change Unless Otherwise Stated)				
	2008	2009	2010	2011
Real GDP	-3.0	-9.0	-3.0	2.5
Real GNP	-2.8	-11.3	-2.5	2.3
Consumer Spending	-1.0	-8.0	-4.0	2.0
Government Spending	2.6	-0.3	0.0	0.0
Fixed Investment	-	-	-	-
Exports	-1.0	-6.0	-3.0	3.0
Imports	-2.1	-10.2	-5.5	3.0
CPI (%)	4.1	-4.0	0.5	2.8
Unemployment Rate (%)	6.3	12.6	15.5	14.6
General Govt. Balance (as % of GDP)	-7.1	-10.7	-10.7	-8.5

Source: AIB Economic Research Unit, September 2009



Tadhg Buckley, AIB Agri Adviser, is pictured at the Macra na Feirme Spring/Summer Seminars with members of Clare Macra na Feirme.



Pictured at the Launch of the Limerick Show are John McDonagh, Limerick Show; Gerry Clifford, Dan O'Connor Feeds; Patrick O'Meara, AIB Agri Adviser; Jim McDonagh & Pat Walsh, Limerick Show; and Pat Enright, AIB Branch Manager Abbeyfeale.



Pictured at the Autumn IFA Livestock Meeting held in Limerick are Donal Whelton, AIB Agri Adviser; Darren Carty, Irish Farmers Journal; Sean O'Leary, IFA Munster vice-president; and Michael Doran, IFA Livestock chairman. Picture courtesy of the Irish Farmers Journal.

The Dairy Market

The market remains extremely difficult with activity low and prices at very depressed levels. The current position is all the more stark given that it has come about less than two years from when prices were at an almost historic high. This is clear when market returns at the beginning of August this year are compared with the returns for the same date in 2007 (see Table 1, the comparisons are in gross milk equivalent terms).

This deterioration in market returns has had a delayed, but inevitably major, effect on farmgate prices. Over the past year, prices paid to farmers have fallen by 24%, 42% and 47% respectively in the EU, US and New Zealand.

Table 1: Comparison of dairy markets returns 2007 - 2009

	World market (c/litre)	EU market (c/litre)	US market (c/litre)
2007	43 to 46	50 to 52	41 to 47
2009	20 to 22	24 to 25	21 to 24

Source: AIB Estimates

There is an additional element of considerable importance to Ireland in this story. The exceptional increase in market prices through 2007 and into 2008 was quicker and more pronounced in the case of dairy commodities than of other dairy products. The Irish industry is more heavily dependent on commodity production than is the industry in most other EU Member States. As a result, dairy prices in Ireland rose more quickly, and to a greater extent, than prices in the Union generally. Inevitably, as a consequence, the downturn has been more pronounced here than on average elsewhere in the EU (prices here are down about 35% at this stage this year).

The average milk price in Ireland this year is forecast to be about 22c/litre (VAT included). This is just about equal to the estimated average cost of milk production here. Thus, for the majority of Irish dairy farmers, income this year will come mainly from returns from other farm activity, direct payments and non-farm income.

As shown above, the drop in milk prices in Ireland over the past year is a universally shared phenomenon. The cost/price development here is not unique either. The US is the biggest milk production area in the developed world and, based on USDA figures for July, the situation in the three largest dairy States (California, Wisconsin and New York) and one of the smaller

Table 2: July cost/price developments in selected US States

	California	Wisconsin	New York	New Mexico
Costs (€c per litre) (excluding depreciation)	32	24.5	30	20.5
Milk price (c per litre)*	16.5	18	18.5	17

*US figures converted at the July exchange rate of €=1.41

Source: USDA

States (New Mexico) is, on average, as set out in Table 2.

Even if the return from farm sales other than milk (equivalent to 3-3.5c per litre, based on figures for previous years) is taken into account, it is only in New Mexico that the overall return is not substantially below the average cost of milk production in the month in question.

The situation in both Europe and internationally is, therefore, very difficult. The important question is whether there is likely to be an improvement in the foreseeable future. While nobody can be certain about market developments in present circumstances, the omens appear to be more positive. The EU is set to maintain intervention up to August 2010. This should provide a floor in the market, admittedly at a relatively low level. Market prices generally have been edging upwards over the past couple of months and there is recent evidence that the pace of improvement may be picking up a little. The cost/price squeeze is beginning to have some effect and this is likely to reduce supplies, especially in the US where, despite an increase in support prices, dairy cow numbers are expected to continue to decline. There is increasing evidence that the worst of the economic recession is over and a return to growth should lead to a significant upturn in demand for dairy products.

The market improvement is likely to be gradual and, almost certainly, we will not see a return to the heady price levels of the second half of 2007. The need to run down stocks will, to some extent, temper the speed of the recovery and the general economic situation is likely to prevent a return to the exceptional prices of two years ago. In any event, any early return to those prices would hardly be in the longer term interests of the market, as those elevated price levels were a factor in the reduction of demand that helped to create the current difficult situation. We should, however, over the next 12-18 months see the re-emergence of markets that will again give a reasonable return to milk producers.



The Agri Banking Market

Patrick Butterly
AIB Agri Adviser, North East

Considerable investment has taken place on farms over the past decade and was particularly strong in recent years, undoubtedly driven by the Farm Waste Management Scheme (FWMS).

The Central Bank Quarterly Bulletins show that agricultural lending grew by €1.017 billion from December 2006 to December 2008, an increase of 23%, bringing total farm lending to a record level of €5.42 billion at the end of December 2008. In addition, a significant level of farm investment was also undertaken from cashflow and farmers own resources, supported by the good profitability levels in the tillage sector in 2007 and the dairy sector during 2007 and 2008.

Despite the difficulties in the economy and contrary to the general perception that banks are not lending, we are still seeing evidence of farm investment taking place, albeit at significantly reduced levels compared to recent years. This is understandable given the very high level of investment on farms undertaken in recent years, particularly in the dairy and tillage sectors, and the current income difficulties now being experienced on these enterprises.

Open for business

AIB is still very much open for business, and is applying the same criteria when assessing loan requests as we did over the last number of years. In a recent extensive independent survey on credit availability to Small and Medium Enterprises, the Mazars report concluded that 8 out of 10 of all enquiries to AIB result in approval of credit facilities.

When a formal application for credit facilities is made the approval rate is even higher at 9 out of 10. The recent publication of this independent report confirmed our own in-house research and data which shows that AIB continues to lend to businesses to the extent outlined. We understand how our support for the farming and business community is critical at this time. Obviously some proposals are unsuccessful but it is reasonable to underline that it is not in anybody's interest, most especially the customers, to support propositions that are not viable in the long term.

Reflecting the fact that some of our customers, particularly in the dairy sector, are experiencing cashflow difficulties, the bank is working with clients to find solutions. In most such cases it may be possible to work out some arrangement, such as moving to 'interest only' for a period. In AIB, we have had plenty of experience of working through such situations with clients, most recently pig farmers where incomes were severely impacted by high feed costs during 2008, and compounded by the dioxin scare at year end. Pig farmers are now back in profit and should stay there for the next 12 months helped by the combination of stable prices and lower input costs. We are now seeing demand for credit returning to this sector to increase production capacity and/or improve production efficiencies.

Where a viable farm business is experiencing cashflow difficulties, the options may include increasing overdraft limits, negotiating a top-up on loan facilities, or indeed restructuring where appropriate for an agreed period to support cashflow. Each individual situation is dealt with on a case by case basis. It must be noted that flexible repayment options whilst appearing cheaper in the short-term could be more expensive over the

life of the loan. Farmers looking to restructure their bank finances should provide a supporting cashflow projection (see page 6). I would recommend that they enlist the services of an agri consultant, Teagasc adviser or their accountant in making the cashflow projection.

Following significant changes in global money markets, as a result principally of the credit crunch the cost of raising cash funding has increased significantly for banks and governments. A key impact is that banks are now increasingly asking their customers to pay this funding premium over their base rates. This has been a source of frustration for customers given the low point at which the European Central Bank reference rate is at present.

Our advice to those experiencing difficulty is to talk to their bank as early as possible. When meeting with your bank take time to prepare and bring information to support your case. If you feel it is necessary, bring along your adviser, accountant or consultant.

Basel is a worldwide convention on standards for credit risk management that impacts on all banks and requires them to increase the level of capital they have to hold for accounts that go over agreed limits or miss payments. These Basel guidelines for breaches of overdraft limits or for loan arrears constitute the main implications for customers. This regulation requires that bank customers be more conscious of managing their bank accounts and contacting the bank in time if they have short-term funding requirements. If customers think they are going to go over agreed limits or miss a payment, they should contact their bank in time to arrange short-term funding.

Since decoupling in 2005, we have seen an exceptional level of volatility in farm incomes, especially in the pig, tillage and dairy enterprises. While to a large extent this has not been caused by the changed system (for instance, incomes in 2007 and 2008 were determined principally by the consequences of the global commodity price spike), undoubtedly we can expect continued volatility into the future. This is something that we all will have to live with and take account of in how we deal with the financing of farm businesses from now on. Dairy and tillage farmers are likely to be pessimistic about the future of their business at present. However, the return to profitability in the pig sector in the past year shows that the down phase of the cycle does and will pass.

My former colleague, Tom Quigley, AIB Agri Adviser for over 30 years, writing in our Spring/Summer edition outlined that profit fluctuations and price cycles were inevitable in a market led environment. I repeat some of Tom's messages in that edition, which advised farmers not to overreact to the high or low prices, not to allow depression set in after one 'bad year' and to view the farm performance over a full cycle (i.e. a three-to-five-year period including a 'good' and 'bad' year).

Farmers can be assured that AIB, with its long tradition of supporting and lending to the farming sector, remains committed to the sector and will continue to support viable businesses.