AgriMatters

AIB supporting the Irish Agricultural Industry

AUGUST 2014

Launching the 2014 Tullamore Show and AIB National Livestock Show were Minister for Agriculture, Food and the Marine, Simon Coveney; Ken Burke, Head of Business Banking AIB; with Rodney Cox Chairman Tullamore Show and Freda Kinnarney Secretary Tullamore Show. This year's Show takes place on Sunday, August 10 in Butterfield Estate. For further information visit www.tullamoreshow.com

A Look at the Markets / Harvest Prospects - 2014

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Welcome to the August edition of *Agri Matters*

Michael Dowling, AIB Agri Strategy Consultant

2014 has been a mixed year so far: weather generally favourable from late spring onwards; milk prices and supply very positive, even if prices are beginning to drop somewhat now; beef prices well down on last year, high by historic standards but with other problems in the market; the sheep sector generally fairly static; pig prices rising significantly as feed costs drop; and cereal farmers looking at lower prices this harvest compared to last year. This, of course, comes after a year in which the outcome varied very significantly between the sectors. All of this is gone into in some detail in our article entitled 'A look at the markets'.

The mixed year that was 2013 had very different impacts on farm incomes in the different sectors. Based on recent CSO and Teagasc information, we have an article looking at farm income in the aggregate last year and at how family farm income varied among the sectors. This very clearly points out the differences between dairying and the other sectors and the continued importance of direct payments to the income position in those sectors.

This edition also contains:

- our usual review of the general economy;
- a preview of the harvest by Fintan Conway of the IFA; and,
- an article by Liam Phelan, one of our Agri Advisors, on key lessons from past investments.

The last mentioned article was written in the knowledge that many farmers have already begun, or are planning, to invest for significant farm development. In that context, since our last edition, AIB has launched a €500 million Agri Fund from which farmers can secure finance for farm development, working capital and asset finance. Furthermore, since our last edition, the Bank has moved to expand its specialist agri advisory service by doubling the number of advisors to twelve. The strengthening of this unique service will further deepen and streamline AIB's relationships with existing and new agri customers. We will profile each of the new advisors in the Ploughing edition of Agri Matters. I wish all of them successful and fulfilling careers in AIB.

Michael Dowling
AIB Agri Strategy Consultant

AIB Doubles Agri Advisor Team

AIB has recently announced that it has doubled its team of Agri Advisors to 12. The bank has recruited three agriculture graduates and three Agri Advisors with strong industry experience. In Limerick, Diarmuid Donnellan joins our team from Teagasc where he was a Business and Technology Drystock Advisor. Bryan Doocey has joined AIB in Cork from Arrabawn where he was Agribusiness Sales Manager and Barry Hyland joins AIB in Cavan from ACC bank where he was Senior Agri Banking Manager. AIB has always sought to support farmers with a specialist understanding of their business and the bank has had a team of dedicated Agri Advisors in place since at least the early 1970s. This strengthening of the team further builds on AIB's knowledge and understanding of the sector as it develops and grows.

Economic Outlook

Year to date, there has been a raft of very strong data published on the Irish economy. The highlight was the National Accounts data for the first quarter of the year which showed that GDP increased by 4.1% and GNP rose by 3.4% on a year-on-year basis.

Every GDP expenditure component, including personal consumption and Government spending, registered positive annual growth, with a particularly strong rise of 7.4% in exports. Business investment was very robust, increasing by 40% year-on-year, while construction spending rose by close to 9%.

Exports have been the main engine of growth in the Irish economy in recent years, most notably service exports, which have had an average growth of almost 8.5% per annum over the past four years. After a marked fall last year linked to the 'patent cliff' in the pharmaceutical sector, the first quarter of this year saw a rebound in goods exports, with a 10% year-on-year increase.

The one disappointment in the National Accounts was the continuing sluggishness of consumer spending, which was up by just 0.2% year-on-year in the first quarter. Spending on goods rose strongly, increasing by 3.1% but this was largely offset by a 2.2% fall in spending on services. Overall though, the National Accounts data indicate that the economy is now on a strong growth path. GNP rose by 1.9% in 2012 and 3.2% in 2013 and this trend was maintained in the opening quarter of 2014.

Figures released for the second quarter of the year point to a continuing strong performance by the economy. Retail sales excluding the auto sector were up by over 4% year-on-year in April/May. Thus, consumer spending may be gaining some momentum, helped by improving consumer confidence and better labour market conditions.

The strong growth of the economy has also seen a big rise in employment over the past two years, with a marked drop in unemployment. This trend is continuing, with the jobless rate falling to 11.6% in June, down from 12% in March. Purchasing Managers Index (PMI) data for Ireland, which are a good barometer of economic activity, have also been very strong in recent months. The services PMI climbed to a seven year high of 62.6 in June, with the manufacturing PMI averaging an impressive 55.5 in quarter two. The construction PMI has been close to 60 in the last three months. Not surprisingly then, housing data have also been strong this year with a large increase in commencements and a big jump in completions up to May. Nonetheless, housing completions are still running well below the estimated demand of close to 25,000 new units per year and this is putting upward pressure on house prices and rents. House prices nationally were up by 10.5% year-on-year in May, while Dublin prices rose by 22%.

The strong performance of the economy is being reflected in the public finances. The Exchequer Returns show underlying tax receipts some €0.5 billion ahead of target at mid-year. A sub 4% budget deficit looks increasingly likely in 2014. Thus, only modest adjustments are likely to be required in the October budget to get the deficit down below 3% of GDP next year.

Table 1: Economic Forecasts – Ireland				
Annual % Change Unless Otherwise Stated				
	2012	2013	2014(f)	2015 (f)
Real GDP	-0.3	0.2	3.0	3.5
Real GNP	1.9	3.2	3.0	3.0
Consumer Spending	-1.2	-0.8	0.5	1.5
Government Spending	-2.1	1.4	1.3	1.5
Fixed Investment	5.0	-2.4	3.0	5.0
Exports	4.7	1.1	5.0	5.0
Imports	6.9	0.6	3.7	4.0
HICP Inflation (%)	2.0	0.5	0.6	1.2
Unemployment (%)	14.7	13.1	11.6	10.5
General Govt. Deficit (as % of GDP)	7.7	6.7	3.8	2.5

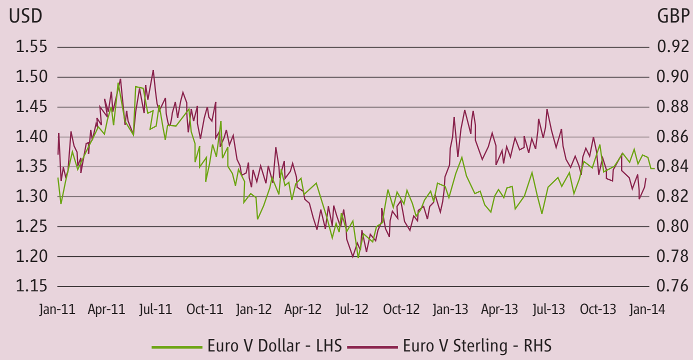
Source: CSO, AIB Economic Research Unit Forecasts

(f) = forecast

The outlook for the economy looks increasingly favourable. Economic conditions in key export markets, such as the UK, USA and Germany, have improved considerably. On the domestic front, the austerity programme which has been in place since 2008 is nearing an end. Sectors which were very depressed, such as construction and retail spending, are starting to recover. Overall, the economy could grow by 3 to 4% annually over the next few years.

On the currency markets, the euro has come under some downward pressure in recent months. This trend could continue over the remainder of the year. The sluggish and lagging nature of the eurozone recovery, the expanding ECB balance sheet and the fact that it still retains an easing bias are factors that are likely to weigh on the currency. Meanwhile, both sterling and the dollar should benefit from the prospect of rate hikes in the UK and US well before the eurozone. As a result, the EUR/USD rate could move down towards the $1.30 level heading into the first half of 2015. Likewise, the EUR/GBP may continue on its downward trajectory, which could see it fall to 78p.

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



Source: Thomson Datastream

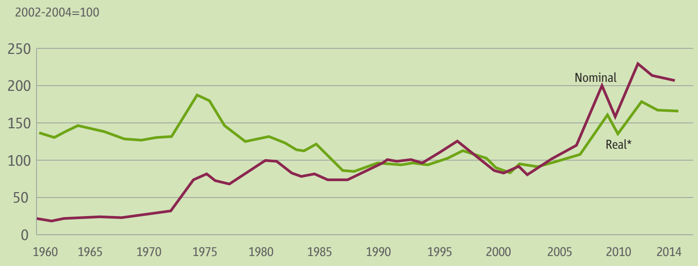
Launching the Irish Grassland Association Dairy Summer Tour 2014 'Strategies for successful expansion' are (L to R) Paul and David Hyland, host farmers; David Kerr, host farmer; Eamonn O'Reilly, Agri Advisor AIB and Bernard Ging, Irish Grassland Association. This years tour will take place on Tuesday the 12th of August in Portlaoise, Co. Laois. For more information visit www.irishgrassland.com

A Look at the Markets

In this article we review what has been a mixed year, so far, for Irish farming.

Volatility continues to be the outstanding characteristic of international commodity markets but it is volatility in real terms at higher price levels than at any other time in the last half century, except during the oil crisis of the 1970s. This is clear from the graph of the Food and Agriculture Organisation (FAO's) food price index - Figure 2.

Figure 2: FAO Food Price Index in nominal and real terms



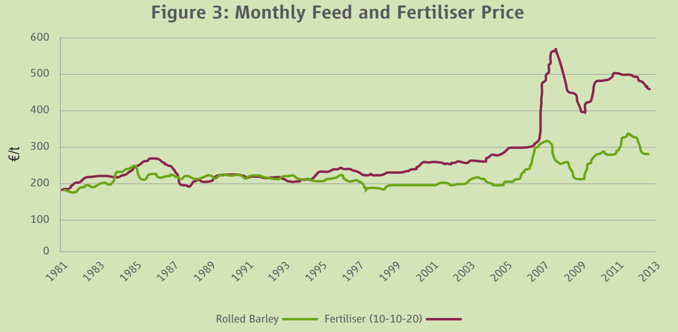
*The real price index is the nominal price index deflated by the World Bank Manufacturers Unit Value Index (MUV)

Source: Food and Agriculture Organisation

The prices of many commodities, especially cereals, have been softening since the third quarter of last year but they are still well above the levels obtained through most of the last 15 years.

The price of farm inputs has, however, been following a somewhat similar trend as is clear from the following graph of feed (rolled barley) and fertiliser (10-10-20) prices over the longer term. In both cases, after a long period of relative stability, the prices of these inputs rose substantially in the middle of the last decade and have been very volatile since. As in the case of the food commodities, feed and fertiliser prices have been softening since the middle of last year, although somewhat less sharply in the latter case, and this trend looks set to continue. USDA predictions are, for instance, for maize prices to be about 8% lower next year and for soya bean meal to be over 20% down.

Figure 3: Monthly Feed and Fertiliser Price



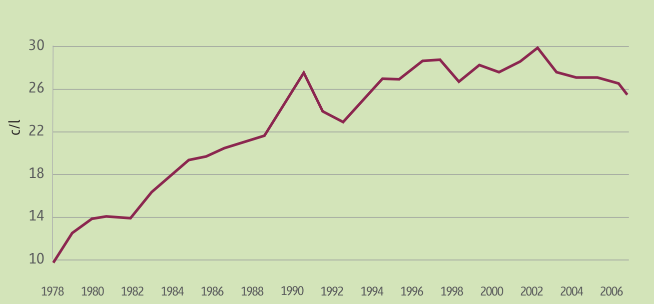
Source: CSO

The Dairy Market

The dairy market has seen perhaps the most dramatic changes over the years. In Ireland there have, for instance, been three quite distinct milk price periods. The first was between our entry to the EU in 1973 and 1986. At that time, under the influence of support price increases from adjustments to the higher Community price levels and green pound changes, milk prices rose very substantially. The second period, from 1986 to 2006, saw relatively flat prices as support prices were virtually frozen and green currencies disappeared for those in the Euro. The third period saw a rapid price rise in 2007/2008 and increased volatility thereafter under the influence of emerging market demand and the reduced level of intervention by the EU in market management. Figure 4 and 5 clearly outline the market price developments.

As an illustration of the extent of the change in the dairy market in the most recent of the three periods, it is worth noting that, in the 20 years prior to 2006, Irish milk prices varied by a mere 9c/litre, between a low of 22c and a high of 31c; in the seven years since, prices have varied between a low of 23c and a high of 39c, a variation of 16c/litre.

Figure 4: Manufacturing Milk Price 1976-2006



Source: CSO

The average price last year was 39.5c/l and that price lasted until the late spring/early summer this year. Market prices for dairy products have, however, been in decline for some months and this is now beginning to be reflected in farmgate milk prices, which will undoubtedly be lower in the second half of the year. The drop in prices is due to a supply surge in the first half of the year, coupled with some slowdown in demand from emerging markets. The expectation is that the increase in milk supply will taper off later in the year and that demand will pick up as China, in particular, comes more strongly on to the market. Indeed, there is already evidence that some product prices are beginning to stabilise. In any event, even in a weakening market, the Irish price should still average between 35c and 37c/litre this year, which would be among the highest nominal prices ever paid here and would coincide with an expected continued fall in feed prices after what looks like, at this stage, a potentially bumper cereal harvest. Milk deliveries are expected to be 5% or so higher this year than in 2013. This, combined with the lower feed costs and prices at the level suggested above, should maintain dairy farm incomes at, or a little above, last year's level.

Figure 5: Manufacturing Milk Price 2007-2013

Source: CSO

It is now expected that some pick up in prices will start in the first half of next year but not to the extent of the uplift in 2013. Into the longer term, the outlook appears to be positive. Output will certainly rise in the EU post-quota, perhaps by over 8%. The US expects to increase by up to 2% a year and there will almost certainly be even bigger increases in New Zealand. At the recent Dairy Industry Newsletter Conference in London, there were estimates that demand would rise by close to 2.5% to 3% a year up to early in the next decade, driven by Asia and Africa (4%) and Latin America (2%), with growth of less than 1% in Europe and the US. China and India were seen as the countries with the greatest supply requirements, with China's self-sufficiency rate set to drop substantially. If these estimates are reasonably accurate, the international market should remain fairly well-balanced, which should maintain the trend of comparatively high milk prices, albeit with continued volatility due to weather and other short-term factors.

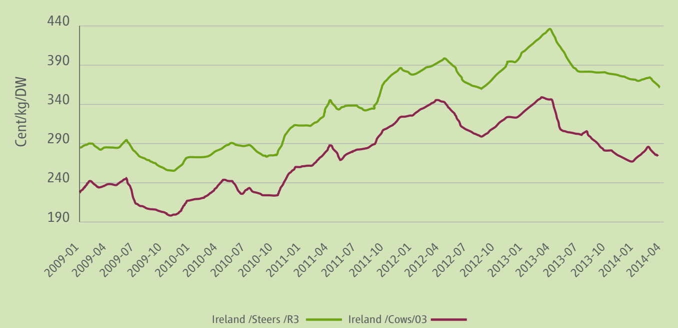
Beef Market

Last year was a difficult and paradoxical one for the beef sector. On the one hand, beef prices were at historically high levels and the value of beef output at farm level was correspondingly high. On the other hand, beef farm incomes were down (see separate article in this edition) due mainly to substantially higher costs on suckler farms and lower direct payments on fattening farms.

The record price level in 2013 was derived mainly from the extremely high prices in the first six months - prices peaked in June and declined fairly rapidly in the following few months and more gradually thereafter, as is clear from the following graph which plots monthly beef prices over the past five years. The first half of last year also saw the third lowest slaughtering of prime cattle here since the middle of the 1990s. This, together, with the very high cattle prices early in the year almost certainly put a squeeze on processors' margins.

Despite the drop in prices over the past year, prices over that period have still been very high by historical standards, as is illustrated in Figure 6. The difficulty has been that the decline in the market since the second half of last year has meant that cattle finishers who bought cattle when prices were still relatively high have had to sell them on to a market giving a lower return than in the previous two years. Also, particularly since last autumn, because of pressures on demand, processors have been applying existing market specifications somewhat more strictly than may have been the case previously. This has put further pressure on the price of certain cattle categories.

Figure 6: Irish Cattle Prices 2009 to present



Source: Bord Bia

There are, however, signs that the decline in price has bottomed out and, of course, the continued fall in feed costs will be of considerable benefit to those overwintering cattle this year. There has, however, been a noticeable drop in consumption during the recession and longer term improvement in the market will be very much tied to the pace of economic recovery, particularly in the UK and the rest of the EU. Throughput at beef processors was up about 14% in the first half of the year, with a somewhat greater increase in the prime cattle kill. Indeed prime cattle slaughterings in that period were at their highest levels since 2007. Higher output, combined with lower feed costs, may keep overall income in the sector in line with last year's, admittedly low, levels.

Pigmeat

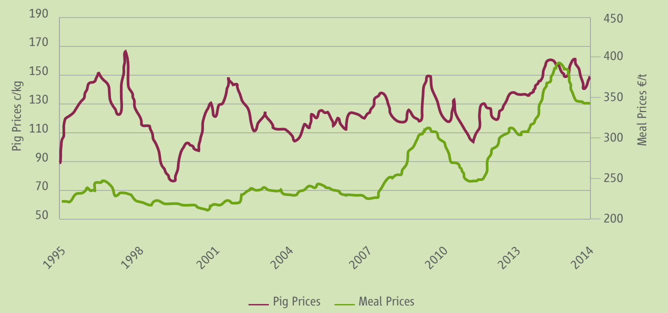
Historically, pig prices have moved in reasonably clearly defined cycles. Over the past ten years or so, the cycles have been somewhat less pronounced, as is evident from Figure 7.

Particularly over the past five years, while the market has been volatile, the underlying price trend has generally been upward. This period has also, of course, coincided with generally exceptionally high feed prices (Figure 7).

In the early part of the year, pig prices in Ireland were running behind the corresponding 2013 levels but, since early May, current year prices have moved ahead and, on a weekly basis, are (as of early July, 2014) some 7.5% up. While well behind prices in the UK, prices here are close to German levels, roughly similar to average EU levels and well above prices in Denmark and the Netherlands. Feed prices have been falling since the second half of last year and, as a result, the feed/price ratio has moved fairly well into profitable territory from the producer point of view. On the basis of the latest USDA forecasts for maize and soya prices for 2014/2015, feed costs should continue to decline in the coming months and, given the likelihood of reasonably firm pig prices over that period, this profitable period looks set to persist.

On the output side, throughput at Irish processing plants is running more or less at the same level as in 2013 and this position should be maintained for the rest of this year.

Figure 7: Irish Pig Prices and Meal Prices



Source: Bord Bia

Sheep

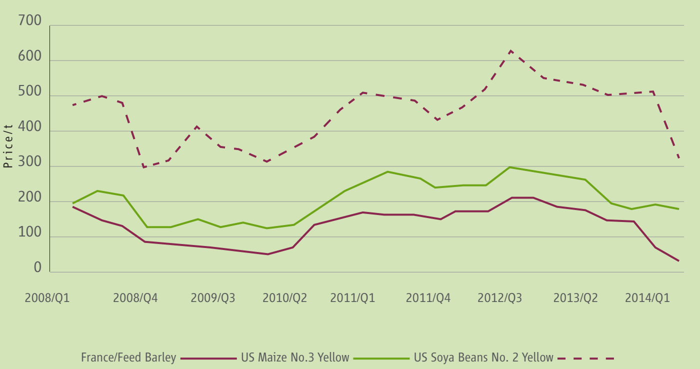
Irish sheep prices had been running ahead of 2013 since the beginning of the year. While current prices have slipped below last years levels, for the year as a whole 2014 prices should finish close to 5% up on last year. Output is about equal to last year's levels and should end the year a bit ahead, as, in recent months, weekly slaughtering levels are noticeably ahead of last year, counteracting the position obtained in the spring. That would make it the highest output figure since 2007, which marked the end of a period of declining output that had lasted for over fifteen years.

Cereals and Soya

World grain and soya prices reached exceptional levels in the 2007/2008 period, and again in 2012/2013. Since then the trend has been downward, and this has accelerated over the past few months.

The international situation has been reflected in the Irish grain market. For instance, Irish green barley prices, which were over €200/tonne after the 2012 harvest, had fallen to less than €150 last year and are not likely to exceed €140 this year. While this may still return some profit on owned land, it makes grain production on conacre very difficult, as leased land prices have been sharply increasing in a reaction to earlier very high grain prices and under some demand pressure from expanding dairy farmers. Fintan Conway's article in this edition deals with the current grain situation in some detail.

Figure 8: Cereal Prices



Source: Bord Bia

Farm Incomes

Two measures of farm incomes in 2013 have been published recently – the final estimate of aggregate farm income in that year from the CSO and the National Farm Survey for 2013 from Teagasc which estimates family farm income.

While the measures are, of course, different they give a broadly similar picture. The Teagasc estimate shows that average family farm income rose by less than 1% last year and the CSO estimate that aggregate entrepreneurial farm income (i.e. farm income after accounting for interest and rental costs) rose by about 1.5%. Both measures, therefore, showed average farm incomes to be relatively static. Averages, however, can conceal a lot.

CSO Income Estimates

The CSO figures showed that the value of farm output rose marginally more than on-farm costs (the value of milk output rose dramatically but there was little change in the value of output from the other sectors; there were substantial increases in feed and fertiliser costs but other costs were relatively unchanged). There was, however, a drop of about 8% in the value of subsidies paid to farmers.

It is interesting to note that the estimate for entrepreneurial farm income in 2013 at €1,735m was just 2% above the average figure for the previous seven years (i.e. since 2006, the first year of the normal working of the single farm payment system). The rise in the cost of living since 2006 was about 8%.

National Farm Survey (NFS)

The Teagasc NFS puts average family farm incomes (FFI) in 2013 at €25,639 which was almost identical with the figure for the previous year but somewhat below the record income recorded for 2011 – see Figure 9.

Figure 9: Average Family Farm Income

Source: Teagasc National Farm Survey

The estimates for the past two years were calculated on a revised sampling base, and the 2011 figure was recalculated on that base. This has the effect of increasing the figures for those three years relative to earlier years. Even allowing for that, the 2013 income level is still the second highest on record in both nominal and real terms. While the gap between average agricultural incomes and those in the rest of the economy has narrowed over the past twenty years, last year's FFI figure was still some 28% behind average industrial earnings. The average agricultural figure does, however, mask some very substantial differences between the different sectors. Also, these figures relate to income from farming; they are not identical with farm household income. For instance, in about 51% of farms, the farmer or the spouse has off-farm employment (down from 59% at peak in 2006) and in about 30% of farms, the farmer has off-farm employment (down from 40% at peak).

As is clear from the table below, the fact that average farm incomes in 2013 were more or less static was due exclusively to the very significant rise in incomes on dairy farms. Incomes on all other farms declined very substantially, indeed dramatically, in the case of sheep, suckler and tillage farms compared both to 2012 and the average of the three years 2010 to 2012.

Table 2: Gross Output and Family Farm Income

2013	Dairying (€)	Suckler (€)	Cattle Fattening (€)	Sheep (€)	Tillage (€)	All (€)
Gross Output	197,788	39,589	54,982	45,223	107,506	86,289
Family Farm Income	64,371	9,469	15,695	11,160	29,907	25,639
% Change in 2013 Family Farm Income on:						
2012	31	-22	-13	-39	-20	0.6
2010-2012 average	15	-16	-4	-40	-20	-2
Direct Payments as % of:						
Gross Output	11	52	33	40	24	22
Family Farm Income	33	167	116	161	87	75

Source: Teagasc National Farm Survey and CSO

The increase in dairy incomes was due to the fact that the substantial rise in milk prices in 2013 (32.5c/litre to 39.5c/litre) was sufficient to outweigh greatly the effects of a fairly sharp increase in input costs. The decline in suckler farm income was due principally to input cost increases, mainly in relation to feed, as the value of output actually rose marginally. The value of output on cattle fattening farms fell modestly, production costs were on average static but there was a significant fall (14%) in direct payments which was the main cause of the income drop. Sheep farms suffered a roughly similar drop in direct subsidies in 2013 and, in terms of its effect on farm incomes, this was exacerbated by a decline in the value of output and a big increase in feed costs. In the case of tillage farms, there was no single major factor in the income decline. A combination of a 7% to 8% drop in the value of output and in direct payment receipts, as well as a small increase in production costs, accounted for the 20% income decline.

As was the case in earlier years, in 2013 direct payments were the biggest single element in farm income in all sectors other than dairying, and, even there, they accounted for almost one-third of income. In fact, in the cattle and sheep sectors, incomes would have been negative without those payments. The sharp drop in incomes in 2013, particularly in the case of suckler and sheep farms, somewhat exaggerates the importance of direct payments in farm income compared to the normal position. For example, the relevant percentage importance of those payments in the three years 2010 to 2012 in the case of those two sectors was 140% and 102% respectively. It is expected that the situation will move back towards normal this year, especially in the case of sheep farms. But whichever way it is looked at, it is clear that, for the majority of farmers outside of the dairy sector, direct payments are of critical importance in maintaining farm incomes and, even within dairying, they are an important element.

Harvest Prospects – 2014

Fintan Conway, Executive Secretary, IFA Grain Committee previews the tillage harvest.

Irish harvest estimates

Another year has passed and the harvest is upon us. Despite good yields last season, falling margins coupled with a difficult and late spring has seen a drop in Irish cereal, oilseed and protein crop sowings. The overall cereal area for the 2014 harvest is estimated to be down by 17,000ha to 280,000ha in comparison to last season.

There was a substantial increase in winter plantings and a good backend last year saw most of the Irish winter crops established in ideal conditions. The overall winter cereal area is estimated to be up by 28,000ha, with wheat sowings up 12,000ha, barley up 14,000ha and oats up 2,000ha. However, the spring sowing campaign got off to a late start due to a cold and wet spring resulting in a significant drop in spring sowings, estimated at 45,000ha. Spring wheat plantings are estimated to be down by 5,000ha, spring barley down by 27,000ha and oats down by 13,000ha.

The recent good weather has boosted crop development but yields are expected to come in below last season's levels. Irish cereal harvest production forecasts for the current season are for 2.1 million tonnes (mt) compared to 2.2mt last year. The cold late spring saw a significant drop off in oilseed and protein crop sowings. The land devoted to pea production is back by about 15%. The area sown to beans is, however, down over 50% while the oilseeds area is down close to 70%.

Table 3: IFA Irish Cereal, Oilseed & Protein Harvest Estimates – 2013 & 2014

Cereals	Area (ha)		Yield (t/ha)		Production (t)		
	2013	2014	2013	2014	2013	2014	Change on 2013 (t)
W Wheat	43,800	56,000	9.6	9.3	420,480	520,800	100,320
S Wheat	14,700	10,000	7.9	6.8	116,130	68,000	-48,130
Total Wheat	58,500	66,000			536,610	588,800	52,190
W Barley	35,200	49,000	9.2	8.65	323,840	423,850	100,010
S Barley	178,000	151,000	6.7	6.57	1,192,600	992,070	-200,530
Total Barley	213,200	200,000			1,516,440	1,415,920	-100,520
W Oats	5,400	7,000	7.8	7.9	42,120	55,300	13,180
S Oats	20,200	7,000	5.9	6.6	119,180	46,200	-72,980
Total Oats	25,600	14,000			161,300	101,500	-59,800
Total Cereal	297,300	280,000			2,214,350	2,106,220	-108,130

Source: IFA

EU production forecasts

On the European front, overall grain output is forecast to increase by 6.8mt (2.3%) this harvest. EU soft wheat production is expected to rise by 7.4mt (5.6%) to 140mt, with maize up 4.7mt (+7.3%) but barley is forecast to be down by 4.6mt (-7.8%) to 54.5mt. Significant recovery is seen in UK wheat production which is expected to supply an additional 2.9mt, followed by French production, which is forecast to increase by 1.6mt. Increased wheat supplies are also seen coming from Poland, Denmark, Hungary, Slovakia, Germany and the Netherlands. Wheat production in the Mediterranean is forecast to fall, with Spanish production down by 1.7mt. As regards European maize production, significant increases are forecast for Hungary up 2.3mt, France 1.2mt and Germany 1.1mt, while Romanian output is expected to fall by 1.1mt. On the barley front, Spanish production in the southern part of the country was badly affected by a prolonged drought and output is forecast to fall by 3.3mt. UK production is also expected to fall significantly, down by 1.2mt but this is due to a switch back to wheat plantings.

Table 4: EU-28 Harvest Production Estimates 2013 & 2014 (million tonnes)

	2013	2014	Change on 2013 (mt)
Soft Wheat	132.57	140	7.43
Durum Wheat	7.89	7.35	-0.54
Total Wheat	140.46	147.35	6.89
Barley	59.05	54.47	-4.58
Maize	63.38	68.03	4.65
Rye	10.05	9.49	-0.56
Oats	8.45	7.91	-0.54
Triticale	10.21	11.87	1.66
Sorghum	0.66	0.81	0.15
Others	5.1	4.22	-0.88
Total Grains	297.36	304.15	6.79

Source: Copa-Cogeca

Market Outlook

International grain and oilseed prices have fallen significantly over the last three months with Irish prices following suit. New crop dried Irish wheat prices peaked briefly in late April/early May at €205/t for November collection with current (late June) values closer to €180/t. New crop barley prices reached €189/t with current values closer to €170/t.

A forecast for increased production across the main producing regions with abundant supplies and a replenishment of carryout stocks has seen investor sentiment turn increasingly bearish of late towards agricultural commodities and, in particular, grains. Grain prices received a temporary boost arising out of the recent geopolitical tensions between Russia and the Ukraine, the cold late spring which affected US winter wheat crops and delayed US maize sowings. Much of this season's increased grain production is expected from maize grown in the northern hemisphere.

Speculative investors have gone increasingly short on contracts of late, banking on a bumper US maize crop to drive international grain prices even lower. However, northern hemisphere maize crops are quite a distance from harvest yet. While the US maize crop was planted somewhat later than normal, much of it has got off to a good start. Recent heavy rain, hail storms and tornadoes have wreaked havoc on some US corn crops but, on balance, the cooler, wetter weather is seen as beneficial towards maize crop development and yields. July will be a critical month as high temperatures during the silking period will trim yields.

While the grain harvesting has already (late June) commenced in southern Europe, the Black Sea and parts of the US, much of the price action still has to take place. Current pricing for feed grains is predicted on the basis of a bumper US maize crop. Weather, between now (July, 2014) and the end of the maize harvest, will have a critical role to play in price direction with attention turning to the southern hemisphere if current yield expectations in the north are not met. Crop reports over the coming weeks will be closely monitored by the investment community and prices are expected to remain volatile.

Farmers the world over are reluctant to sell at current lows and this could see some lift in prices, post-harvest, once store doors close and harvest pressure abates.

Key Lessons from Past Investment Experiences

Liam Phelan, AIB Agri Advisor urges a planned and prudent approach to farm investment.

These are exciting times for Irish Agriculture. Agri-food exports continue to perform strongly, we are entering an era free of milk quotas, the Food Harvest 2020 Report has set the overall strategy for the sector and the medium to long term outlook for agri commodities is generally positive.

Many farmers are investing in their farms to increase output and/or improve efficiency. We have seen significant investment in farm land, infrastructure, buildings, machinery and stock, particularly over the past 12 months. We expect this investment to continue into the future as farmers position themselves to avail of the opportunities presented. As the sector enters another period of significant investment, particularly in the dairy sector, it is perhaps an appropriate time to review and learn from past investment experiences.

Farm Investment 2006-2008

The last period of significant on-farm investment occurred from 2006 to 2008, supported by the grant aid provided under the Farm Waste Management Scheme. It is estimated that gross on-farm investment was over €4.5 billion in that period, peaking at €2 billion in 2008. In addition to the investment undertaken from cash flow and farmers' own resources, lending to the sector reached record levels at this time.

The difficulty for many farmers who invested at that time was that this period of significant investment was quickly followed by a relatively short period of depressed commodity prices, poor weather and a somewhat lengthier period of high costs. This led to a dramatic reduction in farm profitability in 2009 (farm incomes fell by 41% between 2007 and 2009) and many farmers experienced a very difficult period with cash flow stress common on many farms.

Key Lessons

There are some lessons which we can learn from this period, which may be useful for farmers considering future farm investment.

- **Don't base investment decisions on one good or bad year**
  Many farmers undertook investment supported by strong average farm incomes in 2007 and the availability of grant assistance. Decisions to invest in the farm should never be made based only on a good year or on high performance expectations but rather on the longer term likely performance and actual capability of the farm. Our advice to customers is to take a multi annual view and examine the performance of the farm over the previous three to five years taking account of variations in the actual outcome and profitability.

- **Fully cost any investment and allow for over-runs**
  Farm investments often take longer to complete and cost more than originally planned. This was the case in 2007 and 2008 when the cost of steel and concrete increased considerably and added to on-farm development costs. Before undertaking any farm development, it is important to cost the investment fully and it is prudent to include a contingency cost of around 10-20% in all plans. To get a realistic idea of the potential cost involved, and to learn from the experiences of others, it is good advice to take the time to visit similar projects and get quotations from a number of reputable suppliers.

- **Understand the impact on the farm's cash flow**
  During periods of capital investment, good cash flow management is key. While many farm investments will contribute to increased profitability in the longer term, they can place immediate pressure on the farm current account. This is particularly the case where some of the investment is funded from cash flow. Where farm investment is carried out from cash flow, it can compromise the ability of the farm to withstand a cyclical or unexpected downturn in the sector and a period of low margin income. Many of the difficulties in 2009 were compounded by the fact that savings on many farms had been depleted to support farm development in the previous years.

  Before undertaking any farm investment, it is desirable to complete a cash flow forecast to understand the effect of the investment on the cash flow of the farm.

- **Structure loans correctly**
  Ideally, a loan should be structured to match the useful life of the asset being financed. It is important not to put undue pressure on farm cash flow by seeking to repay a loan in an unrealistic timeframe which comes from trying to finance capital expenditure items over too short a period. The shorter the loan period, the higher will be the immediate repayment requirements.

- **Build a buffer fund to support low income periods**
  Volatility has become a feature of the sector in recent years and it is important that farms can rebound quickly from periods of low returns. During periods of higher returns, farmers should seek to build a buffer which can be utilised during periods of cash flow pressure and low income returns. This buffer can take different forms, e.g. building a cash reserve, reducing creditors, improving soil fertility and / or forward purchasing of inputs. Those farmers who undertake significant investment tend to be more exposed to the effects of volatility as savings may be depleted and bank repayments tend to be higher. In 2009, a period of low market returns and higher costs coincided with higher bank repayments on many farms.

Conclusion

The positive medium to long term outlook for the agri sector has pointed to another period of significant investment on Irish farms. It is important that this investment is carried out in a planned and sustainable manner and that adequate time and resources are devoted to the planning process.

The increased level of volatility witnessed on Irish farms in recent years has highlighted the importance of financial planning when undertaking farm investment. It is likely that this level of volatility will continue into the future and it is important that all farm businesses are able to take advantage of the good years, while weathering periods of reduced incomes and low market returns.

It is important that we learn from the past and ensure that any future farm investment does not compromise the ability of the business to survive and prosper in the longer term.