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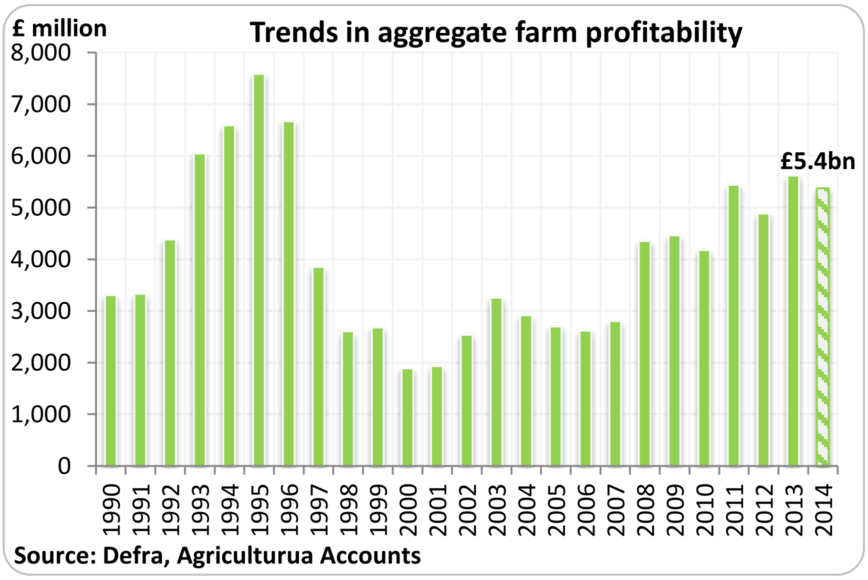
Farm profitability falls following lower commodity prices

Headline figures

Defra has published its first estimate of Total Income from Farming figures (TIFF) for 2014. The TIFF is a measure of the performance of the whole agricultural industry in the UK. A second estimate will be published on 26th November 2014.



Source: Defra, Agriculturua Accounts

The profitability of UK farming fell by 4.4% to £5.4 billion in 2014, after adjusting for inflation. However, 2014 still represents the sixth successive year in which farming profitability has exceeded the £4 billion mark. TIFF is now around two and three quarters (184%) higher than it was in 2000, but is still around 30% below its peak in 1995.

Key drivers behind the fall

The key contributors to the fall in aggregate income in 2014 were increased production offset by lower farmgate prices and reduced payments resulting from the less favourable euro/sterling exchange rate.

A combination of global supply and demand factors and continued intense competition at a retail end has put a downward pressure on farmgate prices across the sectors in 2014. The start of 2015 has shown a continuation of the downward trends in prices across most sectors. For example dairy and pig prices are currently almost 20% below compared with the same period last year and lamb values are also under pressure.

In addition, the stronger pound exerted pressure on the sector's profitability in 2014 and continues to be a critical factor in determining commodity prices (the pound strengthened by 6.7% in 2014 compared with the year previous). The relationship between the pound and euro is vital for both farm income and profitability. A strengthening pound against the euro impacts on Single Payment Scheme (SPS). The exchange rate for calculating 2014 SPS payments was the lowest in seven years. A stronger domestic currency also makes exports less competitive and imports cheaper.

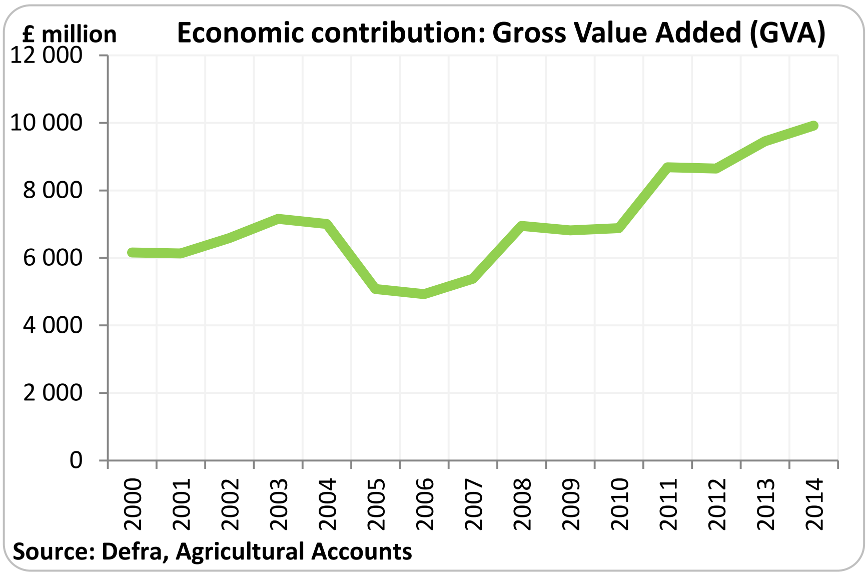
Overall a sector with increasing economic contribution

What continues to stand out from the latest figures is the increasing economic contribution the agriculture sector is making to the national economy in terms of its Gross Value Added (GVA). The NFU emphasised this message in its Back British Farming in a Volatile World report, launched at the

NFU's Annual Conference earlier this year. At the time we stated that the GVA rose by 35% in the five years to 2013.

However, with GVA now reaching almost £10 billion, it means that the sector's contribution to the economy has increased by 43% since 2008. At the same time farm output has grown by 29% to £25.8 billion.

Once again this highlights the importance of farming to the economy and the resilience of the sector during times of uncertainty and volatility.



What is happening to agriculture's cost base?

Despite a modest fall in agriculture's cost base in 2014, farmers have spent almost £16 billion in purchasing inputs over the past year.

The fall was largely due to £555 million decrease in animal feed, the largest contributor to the overall cost base. In 2014 feed prices fell as higher crop production pushed down grain prices. Favourable weather conditions led to good grass growth and reduced the need for animal feed. The value of seeds fell by to £159 million to £708 million. Again the good weather conditions led to no unexpected problems, this was in contrast to 2013 when demand for seeds was high due to the wet weather conditions and a need to re-plant in both spring and autumn. As a result volume levels fell by 8.3% and prices by 11% in 2014.

The value of energy consumed fell by £78 million to £1.4 billion. Declining world oil prices led to a fall in the red diesel price, a reduction of 11 pence per litre between January and December 2014. Volumes were 6.7% lower as there was less land work in the spring.

However, there has been a continuous rise in the overall cost base of the agriculture sector in the long-term and farmers are spending 30% more on purchasing various inputs and services than they did in 2000s.

NFU Comment

TIFF remains a popular barometer of industry performance and the wider figures are regularly used. For example, the NFU has utilised the TIFF datasets for the various campaigns and reports to emphasis the theme of why agriculture is important to the economy. That said, there are shortcomings attached to the TIFF figures, created by its annual and aggregate approach. Although many in the farming industry will work on a crop year basis, TIFF is based on the calendar year. Furthermore, TIFF does not reflect sector specific challenges, particularly given the diversity and increasing volatility observed across the farming sectors. A more accurate picture is given by the Farm Business Income data which provides detail on individual sectors. Nevertheless, we expect to see these headline figures feature in the coming months when evaluating the performance of the farming sector, and particularly emphasising the positive contribution that farming makes to the wider economy and the trends in output and input values.