

FARM RESILIENCE & FINANCIAL PLANNING

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December 2021

THE
ANDERSONS
CENTRE

AGENDA

- **UK Farming: Profitability and Performance**
- **The Agricultural Transition**
- **Profit Requirement**
- **Farm Financial Management**
- **Analysis and Benchmarking**
- **Farm Model Scenarios**
- **Group Work – Scenario Planning & Viability Assessments**

ARE YOU IN CHARGE OF YOUR DIRECTION?

Quiz

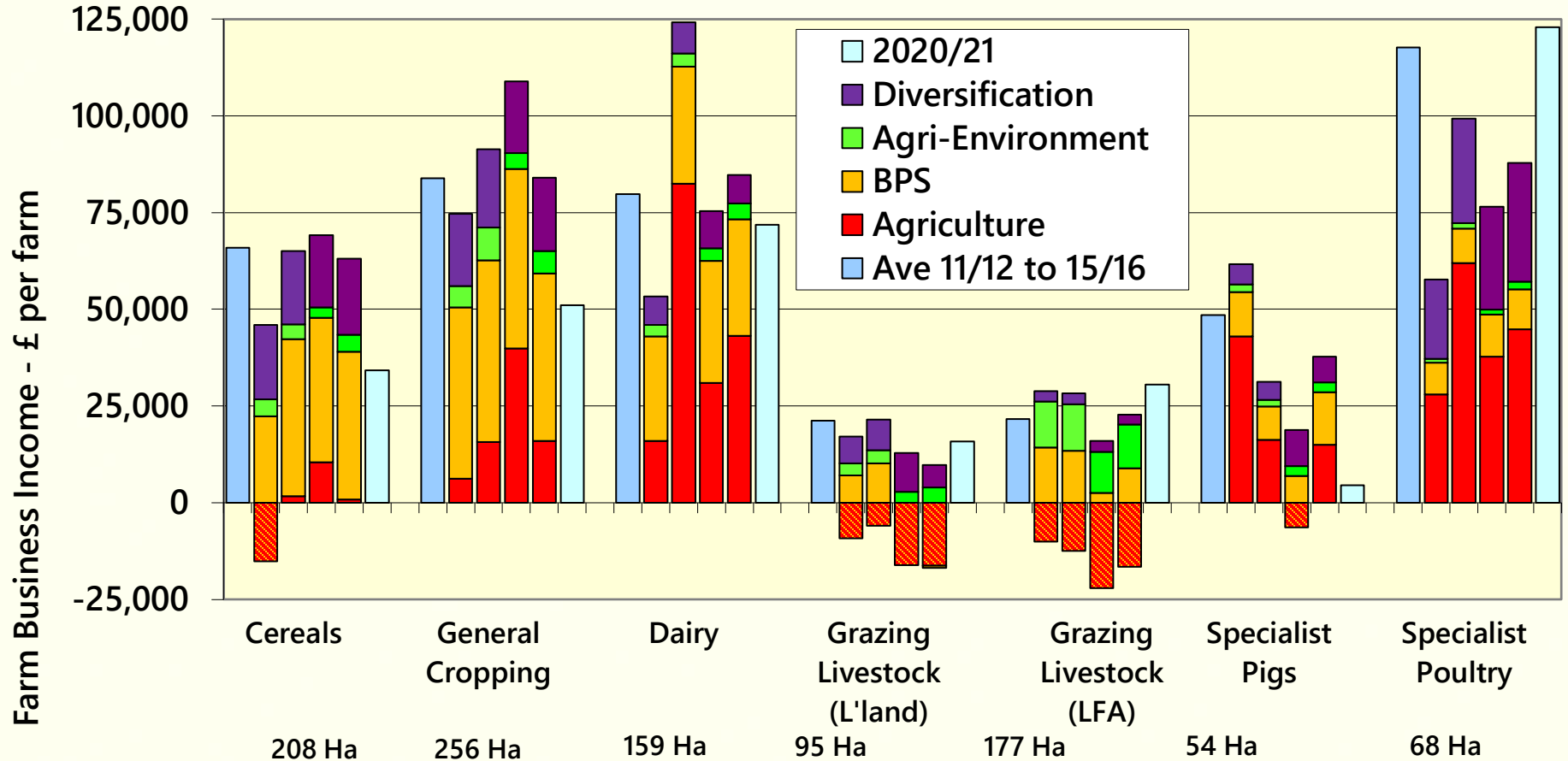
- Take 5 mins to fill out the quiz
- Tick only boxes you can 100% say yes to
- What does your score tell you?

QUESTION	YES
1. Do you have a picture of what your life will look like at least five years ahead?	
2. Have you identified what you will need to meet your retirement needs?	
3. Do you have a plan to develop your skills for the future (e.g. people skills, technical skills, financial skills, leisure activities, off-farm investment options)?	
4. Do you have a written business plan or list of goals you are working towards?	
5. Do you have a written action plan for the week and month?	
6. Are you achieving your desired balance between time spent with family, friends, personal development, leisure, work and business?	
7. Do you meet with key people regularly to review and plan your future direction (e.g. partner, other investors, banker, accountant, consultant, valued friend)?	
8. Do you read a lot and meet with positive motivated people regularly?	
9. Is your farm system, stocking rate and calving/lambing date optimal for your farm? Do you monitor five or six key drivers for achieving outcomes on your farm.	
10. Do you really enjoy what you are doing?	
11. Do you regularly and simply evaluate options?	
12. Do you have an appropriate business structure (e.g. sole trader, company, partnership) and a succession plan and will?	
13. Do you analyse your business returns annually and benchmark them against top performers? (e.g. gross farm revenue, cost of production, % of revenue retained, operating profit, return on capital, growth in equity).	
14. Do you know what profit your farm has to generate to meet your drawings, interest and capital repayments, tax and investment needs?	
15. Do you have an annual budget and a monthly cash flow budget monitored against actuals?	

UK FARMING: PROFITABILITY & PERFORMANCE

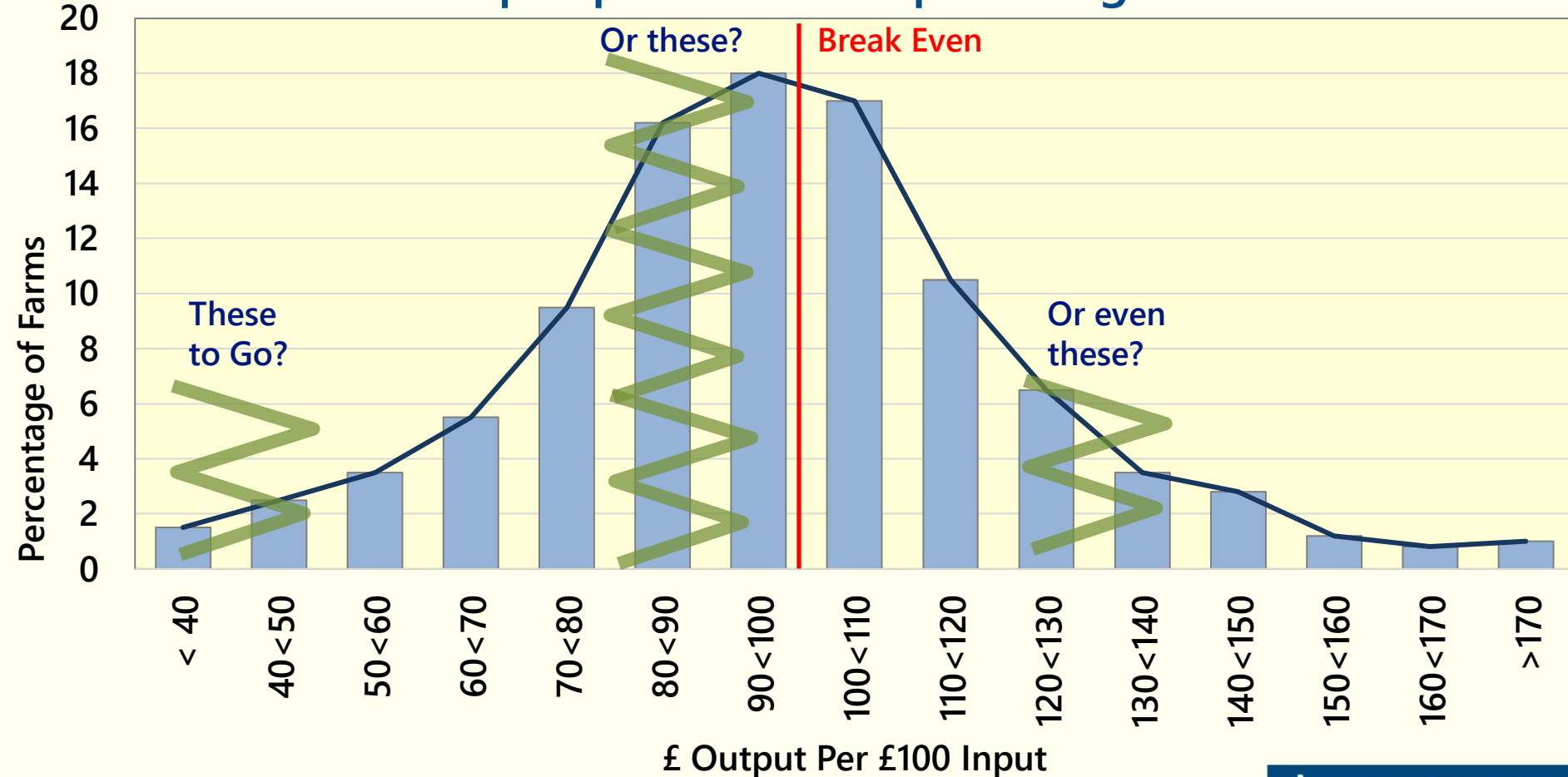
ENGLISH SECTOR PROFITABILITY

Farm Business Income* - 2011/12 to 2020/21



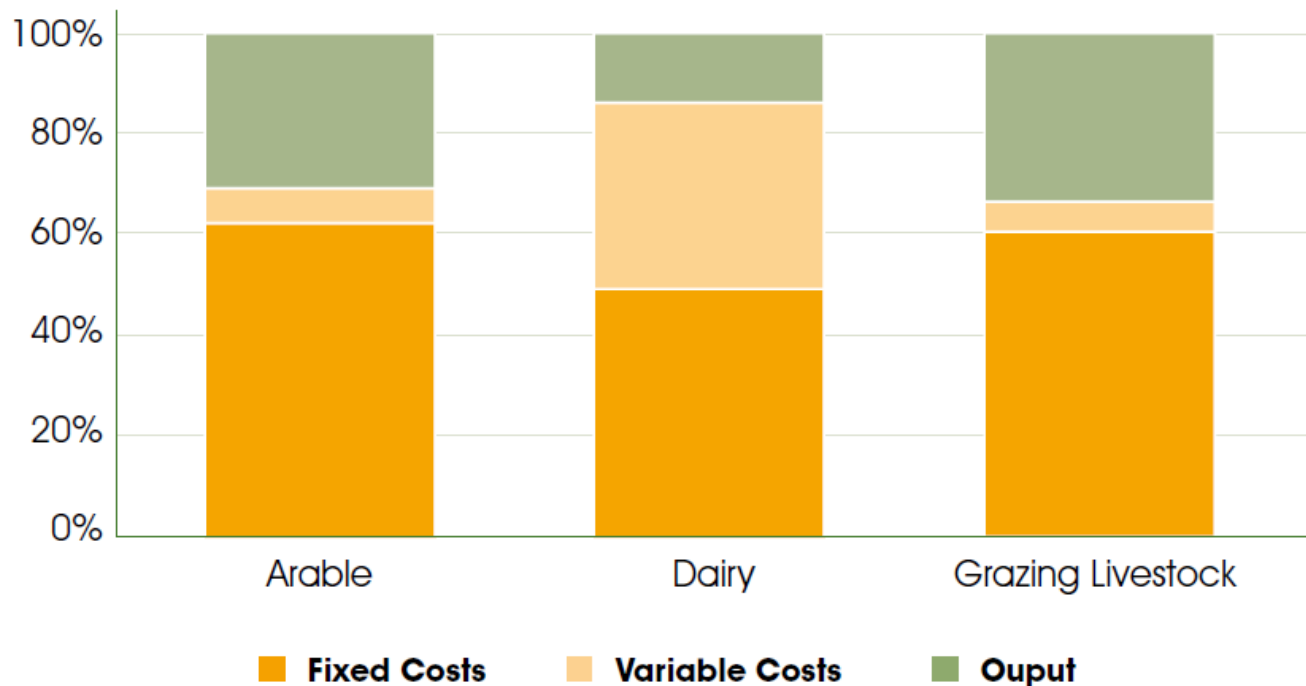
RANGE IN PERFORMANCE

£ Output per £100 of Input - England



RANGE IN PERFORMANCE

CHART HIGHLIGHTING WHERE THE VARIATION IN PROFIT OCCURS BETWEEN TOP AND BOTTOM QUARTILE FARMS



Source: Oxford Farming Conference Paper 2015, Defra

THE AGRICULTURAL TRANSITION

ENGLAND: THE AGRICULTURAL TRANSITION

Deductions:	2021	2022	2023	2024	2025	2026	2027	2028
Up to £30K	5%	20%	35%	50%	65%	80%	95%	100%
£30K-£50K	10%	25%	40%	55%	70%	85%	100%	100%
£50K to £150K	20%	35%	50%	65%	80%	95%	100%	100%
Over £150K	25%	40%	55%	70%	85%	100%	100%	100%

- **Bands work like Income tax:**

160 Ha farm:	35.0	29.5	23.9	18.3	12.7	7.1	1.5	-
£37.3K in 2020	-6%	-21%	-36%	-51%	-66%	-81%	-96%	100%
1,000 Ha farm:	188.9	153.9	118.9	84.0	49.0	14.0	1.5	-
£231.8K in 2020	-18%	-34%	-49%	-64%	-79%	-94%	-99%	100%

- **BPS rules and processes unchanged during Transition**

- but Lump Sum and Delinking in time

DELINKING & LUMP SUM

- **'Lump Sum' capitalises future stream of BPS income through to 2027 into one single payment**
 - will be offered in (early?) 2022 *only* - as a 'retirement option' – business principals must stop farming (can keep 5 Ha and non-ag property)
 - £100K cap on lump-sum. Reference years 2018-2020? Claim in 2015
- **Full scheme details expected soon (?) *Is it worthwhile?***
 - *taxation treatment – income or capital? Tenancy surrender?*
- **'Delinking' breaks link between land occupation and support**
 - won't happen until 2024 (was going to be 2022)
 - a personal right to support for previous claimant (business)
 - *will just happen – no need to opt for it*
 - *potential effects where land occupation changes*

GETTING THE MONEY BACK

- **As BPS phases-out, other schemes take up the funding -**
- **Environmental Land Management (ELM)** – from 2024; Pilots 2021
 1. **Sustainable Farming Incentive (SFI)** – starts 2022
 2. **Local Nature Recovery Scheme**
 3. **Landscape Recovery Scheme**
 - *Countryside Stewardship (CS) continues until 2024 (simplified)*
- **Farming Investment Fund** – capital grants, like CPS
- **Farm Resilience Scheme** – training and advice
- **Farming in Protected Landscapes** – National Parks and AONB
- **Slurry Investment Scheme** – capital grants for stores
- **Skills and Training** – professional body for Ag + benchmarking + R&D
- **Animal Welfare** – payments for going above regulatory baseline
- **New Entrants Scheme** – ‘matching schemes’ etc.

OTHER SUPPORT ~ CAPITAL GRANTS

Farming Investment Fund

- **'Son-of' Countryside Productivity Scheme – two tiers**
 - Farm Equipment and Technology Fund – fixed rate of grant for specified items. Online application
 - Farming Transformation Fund – higher value investment. Two-stage application process
- **Scheme opened November 2021. Runs until 2026**
 - grant rates, thresholds, items etc. all currently unknown – like CPS?

Slurry Investment Scheme

- **New scheme. From 2022 to 2025. Farming Rules for Water**
 - grants to invest in storage for 6 months+ including covers
 - rates of grant and rules unknown

SUSTAINABLE FARMING INCENTIVE

Potential Standards

- Arable & Horticulture - Land + Soils Stnds
- Improved Grassland – Land + Soils Stnds
- Low and No Input Grassland Standard
- Moorland Standard
- Waterbody Buffering Standard
- Farm Woodland Standard
- Agroforestry Standard
- Hedgerows Standard
- Dry Stone Walls Standard
- Heritage Standard
- Farmyard Infrastructure Standard
- Orchards and Permanent Crops Stnd
- Peat Soils Standard
- IPM/Pesticide Reduction Standard
- Nutrient Management/Reduction in Fert.
- Animal Welfare Standard

- Not all Standards may have three ambition levels
- Standards gradually added through to 2024
 - revenue & capital elements
- Those in CS can apply if there is no overlap
- Potentially not a 5-year commitment

RENTS AND ELMS

- BPS has elevated rents and CFA charges (*and other input costs?*)
- Future rental values more closely align to earnings potential
 - good land **or** high public goods potential = high rents
- On average rental levels are likely to fall
 - adjustment over the next decade – upheaval until new equilibrium found
- AHA and long-term (existing) FBTs – Tenant (T) to decide whether to enter
 - but at what level? – T. and Landlord (LL) disagree over ‘ELM potential’?
- For new FBTs
 - LL to make ELM claim so as to be in control (and get income)? – allowed?
 - problems if land manager (T) has no financial stake in agreement
 - parties working together to access ELM payments (+ improvements in soil health, weed burden, rotations, drainage, etc.)

SO WHAT?

- BPS at least halves for English farmers by 2024
 - a simple sum
- Can farm businesses recover this through;
 1. payments under the new schemes? (*but remember, **profit** under these schemes will be lower than BPS, even if payments are the same*)
 2. improved farming efficiency? Including a change in costs (rents + others)
 3. other income sources?
 - is there any sort of 'plan' to do this?
- Some businesses may need an 'exit strategy' if do not change
- Opportunities for the best businesses – expansion and growth

UNDERSTANDING YOUR PROFIT REQUIREMENT

WHERE DOES PROFIT GO?

- Drawings – cash, pensions, other private expenditure
- Tax – Income Tax and Class 2/4 NICs
- Loan Repayments
- Re-Investment – any capital expenditure in excess of the annual depreciation charge
- Long-term sustainability requires an annual cash surplus each year on average to achieve capital growth

PROFIT REQUIREMENT

- Setting yourself a target of what profit you require your business to make ?

	Eg:
- Drawings (Cash drawings, Pension, Life Ins, less capital introduced)	£25,000
- Bank loan repayments (Capital Only)	£18,000
- Tax (Calculated to deliver the above after tax, Include NIC & Income tax)	<u>£ 3,800</u>
	£46,800
- Now calculate your profit requirement for your business	
- Is this above or below your 3 year average profits ?	

QUICK EXERCISE

DOES IT STACK UP ?

**Decide Profit required first,
then manage Costs to achieve it.**

**Profit Requirement = Drawings
+ Tax + Loan repayments**

~~**Profit = Income – Costs**~~

Costs = Income – Profit

FARM FINANCIAL MANAGEMENT

FINANCIAL & MANAGEMENT ACCOUNTS

Financial Accounts

- External (tax)
- Historic
- Legal requirement (set format)
 - capital allowances on machinery for tax
- Whole business
- Purely financial

Management Accounts

- Internal (management)
- Current / future
- By choice (what works and is relevant)
 - depreciation on machinery to show actual cost
 - Valuation change
- More detail – by enterprise
- Physical (yields) and £s

Financial accounts are only of limited help in knowing what is going on in a business – management accounts are more valuable

NON-CASH COSTS

Some things do not appear in the P & L, but need to be considered

Unpaid Labour

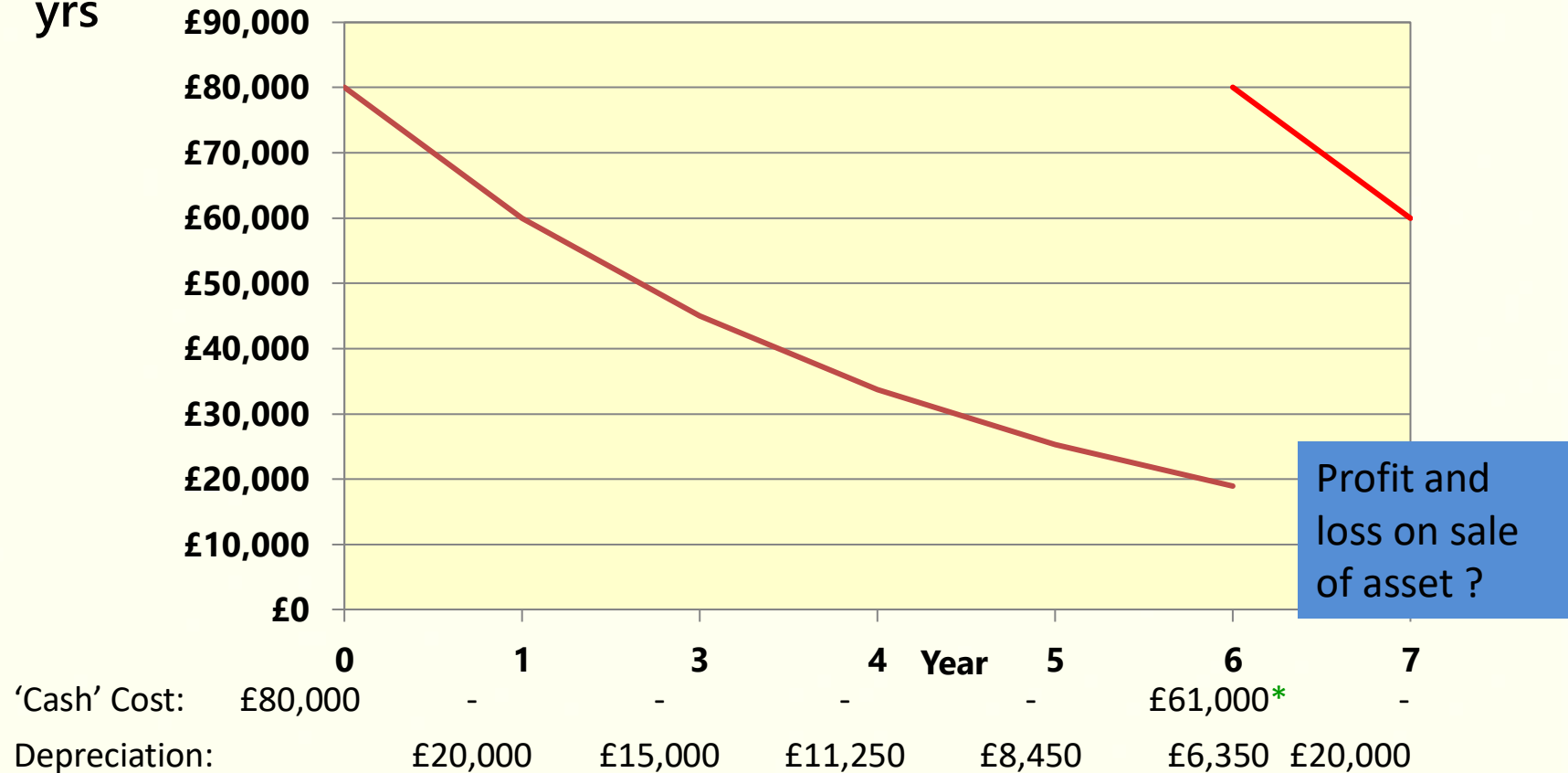
- Farmer, spouse, children, may not pay themselves full economic rate for the work they do
 - thus 'profitability' of the farm will be overstated
- Note, many living expenses are paid through the farm business so requirement for 'drawings' is often low

Land Costs

- Owner-occupied farms will have low/no land costs if farm was purchased many years ago
 - again, 'profitability' of farming operation will be overstated
 - is 'opportunity cost'

MACHINERY DEPRECIATION

- £80,000 tractor, depreciating at 25% per year, replaced after 6 yrs



* Purchase price of £80,000 less £19,000 residual value of old machine

ANALYSING PROFIT & BENCHMARKING

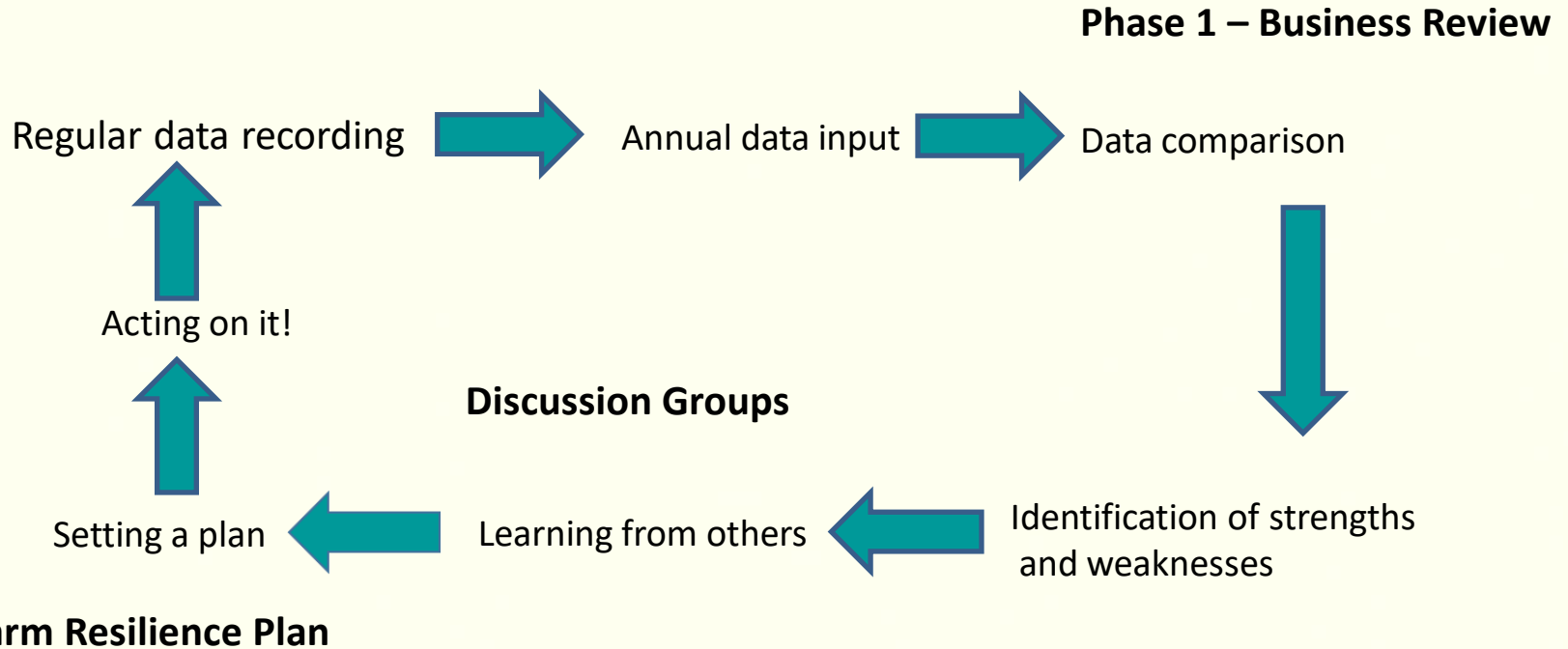
ANALYSIS OF MY FARM PROFIT

- **Internally - within the farm business**
 - am I making more than last year? / the five year average?
 - is there a reason for this – external factors?
- **Externally – comparison to the others**
 - possibly more useful – a business' profits may be improving, but just from awful to very poor
 - are my profit levels (per Ha, per litre, per head, total overall) comparable with similar farms?
 - is my business structure (costs) in line with industry averages – proportional analysis and costs of production?
 - is my Return on Capital adequate?
- **Need to ensure figures are produced on a comparable basis**

FARM BENCHMARKING

- **Just a fancy name for 'comparing against others'**
- **Possible to benchmark with any measure – as long as it's prepared on a consistent basis**
 - unit costs of production (ppl, ppkg, £/hd, £/ha, £/t etc)
 - farm profit, Return on Capital, balance sheet ratios etc.
 - Physical Key Performance Indicators (reared %, yield from forage, output/man)
- **Why?**
 - identifies strengths and weaknesses
 - evidence for an action plan
 - annual review
 - accountability of external advice

THE BENCHMARKING CYCLE



PROPORTIONAL ANALYSIS

- A relatively quick and simple way of analysing a business to find areas for deeper investigation

	Target %
Total Output	100
Direct (Variable) Costs	30-35
Gross Margin	65-70
Labour	15-17
Power & Machinery	15-17
Other Overheads, Admin, Property	5-6
Total Overhead (Fixed) Costs	35-40
Pre Rent and Finance Surplus	30-35
Rent & Interest	15-17
Profit	15-17

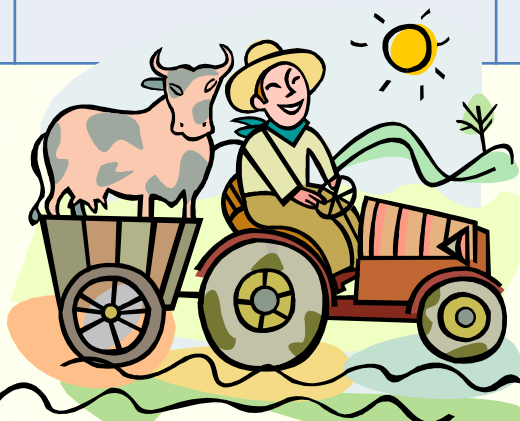
RETURNS

- **Return on Capital is the litmus test for all businesses**
 - not discussed enough in farming
- **Problems around consistent and meaningful calculation**
 - high land values skew figures
- **Businesses of owning land and farming land should be divorced**
 - impute a true rent in all RoC
- **Also impute a cost of all unpaid manual labour**

WHAT IS THE VALUE OF YOUR TIME ?

Time spent on management provides higher return.

	Manual tasks <i>(milking, tractor driving etc.)</i>	Operational management <i>(feeding and fertility planning, etc.)</i>	Strategic management <i>(long term planning, business management)</i>
Value of 1 hour work	£10	£50	£500



QUICK BREAK

GET INTO GROUPS

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