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NEW CALCULATIONS ON COST OF NORTHERN IRELAND SUCKLER BEEF PRODUCTION

DARD, responding to a request from LMC and the Red Meat Strategic Forum has developed a new method to calculate suckler beef production costs using Farm Business Survey data. The Farm Business Survey collects data from a random selection of commercial farms in Northern Ireland. The calculated figures cover the six year period from 2006/07 to 2011/12. They provide an average cost of production on a per kilo basis across the suckler beef supply chain and details of these costs are outlined in this issue of LMC Quarterly. In addition there is a brief article from CAFRE on the importance of monitoring your own production costs and outlines some practical measures that can be taken to reduce costs.

AVERAGE SUCKLER BEEF PRODUCTION COSTS

THE Farm Business Survey for the 2011/12 accounting year shows that the cost of producing beef from the suckler herd was £3.82/kg deadweight on average in Northern Ireland. This was six per cent ahead of previous year levels and was 70p/kg higher than the average deadweight price for suckler origin cattle in the 2011/12 accounting year.

The gap between these costs and farmgate prices raises concerns about the viability of suckler beef production. These concerns are heightened by the fact that these costs exclude any allowance for producers' own labour, land or working capital. The figures serve to highlight the continued dependence of the industry on the Single Farm Payment and any sources of off-farm income to cover the shortfall in NI suckler-beef returns.

Looking into the detail shows that variable costs of beef production (feed, forage and fertiliser) have increased by 45 per cent between 2006/07 and 2011/12. For the accounting year 2011/12, variable costs were up seven per cent on the year.

Fixed costs (excluding depreciation) increased by 32 per cent between 2006/07 and 2011/12 as a result of the increased cost of fuel and building / machinery repairs among other developments. Depreciation charges increased by 29 per cent between 2006/07 and 2011/12 and account for a substantial proportion of overall production costs. It is important to note that these costs are generated by a combination of current and historical capital investment in machinery and buildings. Other income sources like the Single Farm Payment and Farm Nutrient Management Scheme have driven some of that investment. For this reason, depreciation is itemised separately in Table 1 so that producers can clearly see its contribution to overall costs.

The period covered by these Farm Business Survey accounts ended in the spring of 2012. The reality is that costs have continued to rise since then with feed prices rising sharply over the summer and into the autumn of 2012. Producers will also have found it difficult to farm as efficiently as previous years given the impact of the weather on grass and forage availability.

These figures, although not very encouraging are not surprising given the lessons of the 2007 Red Meat Industry Task Force report. The costs outlined in this issue are an average for the entire suckler beef sector and they give an excellent indication of changes in cost over time. However, readers must also bear in mind that there is a wide range in efficiency and profitability across the sector and whilst these average figures capture that range, there are farmers who are making progress with their efficiency and improving their margins. The figures should be interpreted in that context.

While these average figures are a good benchmark, it is important to bear in mind that each farm has its own cost of production figure and that is the figure that counts. All producers should consider participating in the CAFRE benchmarking scheme with the aim of monitoring costs to improve efficiency and increasing returns.

Table 1. Fixed and Variable Costs for Suckler Beef Producers Excludes Land, Labour and Working Capital (£/KG DW)

Costs / Year	06/07	07/08	08/09	09/10	10/11	11/12
Variable	£1.19	£1.27	£1.48	£1.61	£1.61	£1.72
Fixed Excl Depreciation	£0.95	£0.96	£1.01	£1.14	£1.15	£1.25
Sub-Total	**£2.13**	**£2.22**	**£2.49**	**£2.74**	**£2.77**	**£2.97**
Depreciation	£0.66	£0.67	£0.69	£0.81	£0.86	£0.85
Total	**£2.80**	**£2.89**	**£3.18**	**£3.55**	**£3.62**	**£3.82**

Figures may not add due to rounding

SUCKLER BEEF PRODUCTION COSTS

THE viability of NI suckler beef production and the reliance of the industry on the Single Farm Payment is highlighted in the new cost of production analysis undertaken by DARD on behalf of the Red Meat Strategic Forum.

Figure 1 shows how the average cost of production of beef from the suckler herd in Northern Ireland was £3.82/kg for the 2011/12 accounting year. The equivalent figure in the previous year was lower at £3.62/kg. This represents a year-on-year increase of six per cent. The equivalent figure in 2006/07 was £2.80/kg.

Furthermore, producers need to consider that £3.82/kg is not a full break-even price for suckler beef production. These calculations do not take into account the cost of farmers' own labour or the income forgone on own land used (rent) or own money invested in the enterprise (interest). When considering the cost figures presented in this article, producers need to bear in mind these additional costs and what they consider to be an adequate return (See Box 1).

Nonetheless, these figures provide a useful starting point from which to consider developments in costs on an annual basis, what this means for producers and for the industry generally.

Variable Costs

Variable costs are those costs which can both be readily allocated to a specific enterprise and will vary in approximately direct proportion to changes in the scale of that enterprise. These costs include items like concentrates, fertiliser, medicines and herd replacement. As production increases, these costs will also increase.

Over the last six years there have been substantial increases in variable costs. In 2006/07 total variable costs of beef production amounted to £1.19/kg. Since then this figure has increased by 54p/kg to £1.72/kg (+45%).

Figure 2 tracks changes in variable costs over the last six years. Feed costs such as concentrates and forage have generally accounted for about three quarters of all variable costs in recent years and about one third of total suckler-to-beef production costs. Forage costs include fertiliser, and contractor inputs and covers grazing and conserved fodder. The cost of concentrates has increased by 46 per cent over the period, with the cost of producing forage up by 53 per cent.

This increase reflects the outworking of a number of trends: rising unit input costs, developments in on-farm efficiency, alterations to production systems and the weather. It may be the case, for example, that while input costs have increased substantially since 2006/07, improved efficiency in the use of these inputs or a change in production methods may have meant that the increase in production costs is somewhat tempered.

DARD animal feed statistics show that the average cost per tonne of feedstuffs (based on concentrate equivalent) has risen by 65 per cent between 2006 and 2011 (all farms). However, greater efficiency in the use of feedstuff or changes to production methods generally will have helped reduce the overall impact of these higher unit costs on total production costs.

Fertiliser costs (per tonne) have risen by 112 per cent between 2006 and 2011 (*Source: DARD Fertiliser Statistics*), but fertiliser usage (all farms) was 23 per cent lower in 2011 compared to 2006, meaning that the impact of higher fertiliser prices was offset by reduced usage when it comes to overall costs.

When comparing one year with the next it is also important to consider the impact of the weather. This year is an excellent case in point. Higher per unit input

BOX 1 WHAT COSTS ARE INCLUDED?

The figures used to calculate the cost of suckler beef production in NI are from farm enterprises that rear and/or finish suckler calves. These costs are for a combination of steer, heifer and young bull production including suckler cow maintenance costs.

These costs include:
- Costs of purchased inputs
- Depreciation costs
- Bank interest and rent
- Herd replacement costs

These costs exclude:
- Unwaged family labour
- Opportunity cost of own land
- Opportunity cost of Working Capital

With no provision for hidden costs in these figures, producers therefore need to consider that the enterprise must also cover the cost of their own labour, land and working capital.

On any farm business there may be a number of different enterprises. For example, a suckler producer may also be involved in lamb production alongside a broiler breeder operation. Care is taken in the Farm Business Survey to ensure that costs for each enterprise are allocated correctly and proportionately.

Figure 1. Suckler Beef Production Fixed and Variable Costs - 2006-2012

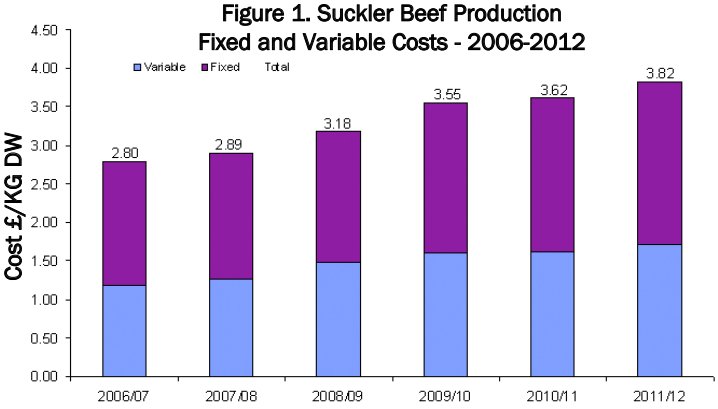
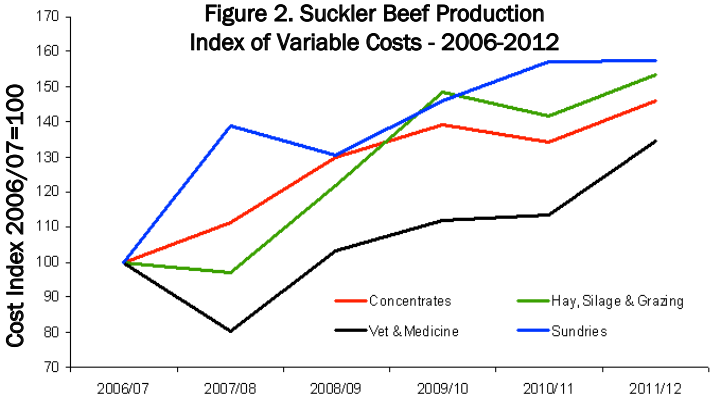


Figure 2. Suckler Beef Production Index of Variable Costs - 2006-2012



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CONTINUE TO RISE IN 2011-12

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costs have been magnified by the poor weather and lack of grass which has made producers more dependent on bought-in feed with beef concentrate sales up by 35 per cent during July and August. The full impact of these effects will be seen when production costs are re-calculated for 2012/13.

Fixed Costs

Fixed costs are those costs that do not vary with small changes in the scale of individual enterprises or cannot be readily allocated to individual enterprises. These include costs such as depreciation on fixed capital and machinery, upkeep and running of machinery, fuel, hired labour, conacre rent, rates and building repairs. Increasing fuel costs has been a significant factor on farms in recent years. The price of agricultural diesel has increased by 70 per cent between 2006 and 2011 *(Source: Dairyco)* and this obviously has contributed to the 58 per cent increase in machinery upkeep and running costs between 2006/07 and 2011/12. The cost of building repairs have also increased, possibly because of increases in the cost of building materials.

Another factor which will have driven increases in fixed costs is increased investment in machinery and fixed capital, which creates increased depreciation costs. This may be driven by higher unit costs of investment, greater investment activity or a combination of changes in both. Nonetheless, the higher costs beg the question: why would producers consider increasing investment in a beef enterprise at a time when they are engaged in loss-making production?

The explanation is likely to be that some of this investment was probably driven by the need to comply with the nitrates directive or other cross-compliance requirements. Failure to adhere to these standards could put at risk the producer's Single Farm Payment and membership of assurance schemes.

Financial assistance in the form of grants and subsidies has funded some capital investment in recent years (see box 2 below). Likewise, significant tax incentives on the purchase of new plant and machinery will perhaps have encouraged some producers to invest more heavily than would otherwise be the case.

Nonetheless, increased capital investment and the rising fixed costs associated with these fixed items certainly have driven-up overall costs in recent years. It is also important to consider the importance of sustainable investment in fixed capital and machinery on farms to help improve efficiency, safety and ensure compliance with environmental and assurance standards.

Figure 3. Suckler Beef Production Index of Fixed Costs - 2006-2012

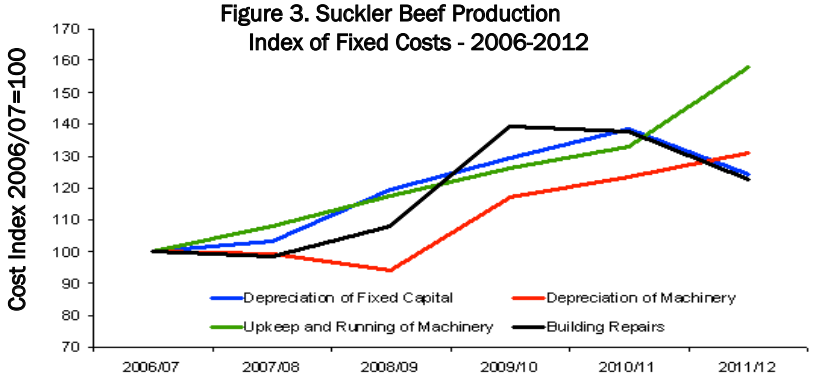
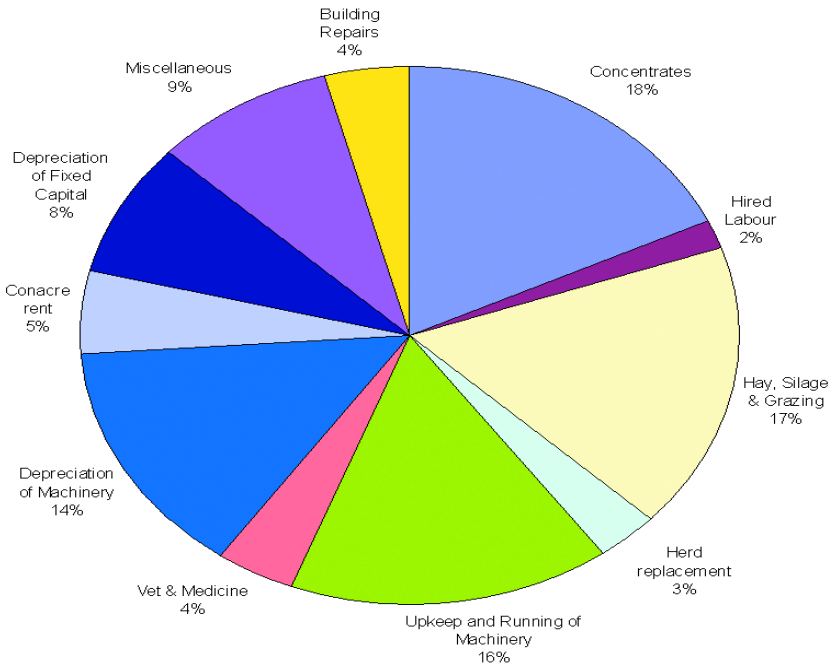


Figure 4. Suckler Beef Production Breakdown by Cost Centre - 2010/2011



BOX 2 DEPRECIATION

Depreciation on fixed capital and machinery contributes significantly to overall farm costs. Depreciation costs are driven by a combination of current and historical investment in capital. For example, £30,000 invested in a slurry tank in 2009 will generate depreciation costs until 2018. Similarly, £60,000 spent on a new tractor in 2010, will also generate depreciation costs in subsequent years.

Depreciation is a real cost that the industry must carry. However, a subtle, yet important point about these figures is that capital investment in the suckler enterprise is not entirely funded by the enterprise itself, with other income streams such as the Single Farm Payment (SFP), Farm Nutrient Management Scheme (FNMS) and Farm Modernisation Scheme playing a part. For example, much investment in fixed capital prior to 2011 was driven by the Nutrient Management Scheme which was established to help farmers comply with the Nitrates Directive. In total £121.4 million in FNMS grants was provided to all farmers (not just beef) between 2006-2008 and the increase in fixed assets depreciation costs must be considered in the context of financial assistance under that scheme.

It is also likely that some investment in machinery and fixed assets has been driven by improved SFP receipts associated with the weak pound from 2009-2011. This coupled with tax incentives may have encouraged more investment in machinery and fixed assets during that period which in turn drives up depreciation costs in subsequent years. With this in mind, care should be taken in the interpretation of these figures given that depreciation is a significant component in these overall costs.

MARGINS REMAIN TIGHT FOR SUCKLER BEEF PRODUCTION

THE Farm Business Survey figures which outline the costs of production for suckler beef enterprises over the last six years, help explain the ongoing lack of profitability in the beef sector.

Figure 5 shows a comparison between suckler beef production costs and farmgate prices paid for suckler origin cattle. The red line shows the average farmgate price paid for prime suckler-origin beef (*source: Price Reporting*). The green bar shows costs, excluding depreciation, while the pale blue bar shows depreciation costs. These costs do not include a return on farmers' own land, labour and working capital.

The figures for 2011/12 show how the average enterprise lost 70p/kg. In 2010/11, the average loss was 98p/kg, with a loss of 92p/kg generated in 2009/10.

The figures show that excluding depreciation, producers just about covered their variable and fixed costs last year. In previous years, average prices did not cover average costs even when depreciation was excluded.

The figures once again demonstrate the dependence of the industry upon the CAP payments to provide producers with an income for their labour and to cover the opportunity cost of using their own land (setting or alternative enterprise use) and interest forgone on cash that is tied-up in the suckler beef enterprise.

This ongoing dependence on the SFP should give pause for thought, not just to individual producers, but to the industry generally, given that the current round of CAP reform is nearing completion.

Furthermore, the failure to cover variable and fixed costs is a concern. It has been stated elsewhere in this issue that some of the depreciation costs attributed to the suckler enterprise have been driven by historical investment that was part-funded by grant aid such as the Farm Nutrient Management Scheme (FMNS).

However, these figures also show that there is little or no room in the price received to fund farm investment. With this in mind, there will be a clear problem in attracting new entrants to the industry unless producers receive continuing support from the CAP, other government subsidies or increased margins.

Ongoing investment on the farm is often essential whether the motivation is to drive efficiency, or concerns around animal welfare, the environment or farm safety. In the future, as in the past, this type of investment will not necessarily happen unless there is a significant support for producers such as the FNMS or improved margins.

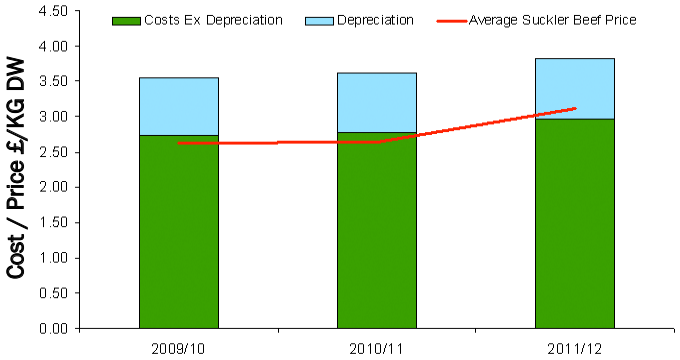
From a strategic perspective, for the future of the industry, this is a significant concern.

When it comes to profitability, individual producers have greatest scope to influence the cost side of the equation, as well as making sure to maximise revenue

With this in mind, in the quest for profitability, producers must continue to sustainably drive down costs where possible whether these are in the form of variable or fixed costs.

In a year like 2012 this must seem like an impossibility. However, there is help out there in the form of CAFRE and AFBI who are on hand to give producers helpful advice and support which may help to improve viability. The CAFRE Benchmarking Scheme and KTT programmes are open to all farmers, including suckler-to-beef producers. Participating producers can benchmark their farm against similar enterprises to gauge their own performance and identify improvement measures. In the context of these figures, this is a very worthwhile exercise. Enclosed is some additional information from CAFRE on actions that can be taken by producers to manage costs.

Figure 5. Suckler Beef Production
Average Costs v Average Farmgate Price Paid for Suckler Origin Beef



ABOUT THE FARM BUSINESS SURVEY

SINCE it began in the 1930's, the Farm Business Survey has provided information on the physical and economic performance of farm businesses in Northern Ireland. It is carried out by Policy & Economics Division of the Department of Agriculture and Rural Development (DARD), and is supported by the farming unions. Currently, 380 farm businesses participate in the survey on a voluntary basis. When new farm businesses are required for the survey they are randomly selected from the census register of farm businesses in Northern Ireland.
Farmers who take part in the survey provide their accounting information on a confidential basis to DARD staff who visit their farm to collect the necessary data. The co-operation of farmers who participate in the survey is greatly appreciated, both for the information it provides on income levels and for the contribution it makes to the knowledge of farm economics. Information from the survey is used to serve the needs of farmers, farming organisations, government, and academic researchers. Further details of the survey and the main annual publications produced from it are available at:

http://www.dardni.gov.uk/agricultural-statistics-farm-business-survey.htm