Farm Advisory Service

National Advice Hub
T: 0300 323 0161
E: advice@fas.scot
W: www.fas.scot

January 2023

News in brief

2022 – A year like no other!

Following on from Brexit and Covid, we all looked forward to 2022 being a 'normal' year but with three new prime ministers, four chancellors, a new monarch, a war in Europe, highest recorded temperatures, avian flu decimating farmed and wild bird populations, a deepening cost of living crisis and strikes not seen since the 1970s; 2022 has proved to be anything but.

As our livestock, arable and dairy articles highlight despite milk prices climbing to the highest on record and sale prices continuing to stay strong for arable and livestock sectors, rising input prices particularly feed, fertiliser and fuel have steadily been eroding margins. This, coupled with interest rates rising by 3.25% since last December, many, especially intensive livestock producers with soaring feed and energy bills are questioning if they still have a future in the industry which could have far reaching implications for food security and rural economies.

As the industry journeys to meet net zero targets, our carbon roundup highlights the progress so far with strategies to reduce carbon footprints and the emerging role of carbon financial markets in funding carbon sequestration. While Defra's support packages are being closely tied to environmental management, Scottish Government's National Test Programme (NTP): Track 1 – Preparing for Sustainable Farming (PSF) literally puts the focus on the ground up with the introduction of support payments for soil analysis and nutritional management advice, coupled with grants for up to date baseline carbon audits and mitigation plans.

While global trends show that Scotland is not alone in its economic struggles as the fallout from the ongoing war in Ukraine continues to reverberate around the world; going forward, how businesses adapt to changing circumstances will be the key to individual success.

Contents

This month's editor:
Christine Beaton

Merry Christmas & Happy New Year

from all the Agribusiness News Team

SAC CONSULTING

Scottish Government
Riaghaltas na h-Alba
gov.scot

Round up of 2022

Seasonal workers scheme 30,000 cap retained

Last Christmas, to ease the labour crisis caused by Brexit/Covid, the UK Government announced a 3-year extension to the Seasonal Workers Scheme. While horticultural workers can apply for a 6-month visa, poultry workers are limited to a 3-month visa from the 18th Oct – 31 Dec each year.

New slurry regulations

New regulations around muck and slurry spreading, are to be phased in over the next five years. The new regulations have been designed, under consultation, to optimise nutrient management on Scottish farms; reduce leakage and pollution from slurry & digestate; and reduce emissions associated with slurry and digestate storage and spreading.

The regulations include the following measures:

- Splash plate slurry spreaders were phased out 1st January 2022, Broadcast spreading with splash plates are being phased out in preference of precision spreading equipment e.g. trailing shoes and dribble bars;
- Farms must have slurry storage for at least 22 weeks for cattle and 26 weeks for pigs, and;
- Tightened restrictions on the distance of silage bales, bulk bags, silos, slurry or digestate storage from water, and construction standards.

Red diesel regulations changed

On the 1st April, the DVLA's rules for use of red diesel changed. Red diesel must now only be used for an approved agricultural purpose, and the vehicle must be registered as an agricultural vehicle and allowed to use red diesel.

SACGS focused on reducing ammonia emissions

On the 26th April, the Sustainable Agriculture Capital Grant scheme opened for just 6 weeks. This year's max £20,000 grant scheme focused specifically on low emission slurry spreading equipment and slurry store covers. The final date for claims is midnight on the 28th February 2023.

Planning for Net Zero

In December, in order to help combat climate change and restore nature, the Scottish Government have published a revised draft National Planning Framework 4 (NPF4) which sets out sustainable policies against which planning applications would be assessed for the next decade.

Preparing for Sustainable Farming

Under the Scottish Government's National Test Programme (NTP): Track 1 – Preparing for Sustainable Farming (PSF) businesses with an online Rural Payments and Services (RPS) account can apply for funding up to £500 for a carbon audit and up to £30 per hectare for soil testing (up to 20% of their Region 1 land in one year) for pH, phosphate, potash, and carbon. A minimal soil sampling allowance of £300 – for small businesses with region 1 land.

Short Term Lets Licensing Scheme

From October 2022, new hosts must apply for a licence and all existing short term let hosts must have applied for a licence by 1st April 2023. For further guidance, click here.

Avian Influenza (Bird Flu) Update

Following the announcement of the UK wide Avian Influenza Prevention Zone across Great Britain. Keepers of all birds (including pet birds) are advised to familiarise themselves with the avian flu advice at www.gov.scot/avianinfluenza and report suspicion of disease to your local APHA Field Services Office.

Looking into 2023…

New Land Reform Bill

The Scottish New Land Reform Bill expected to be introduced by the end of 2023. Proposed measures include the introduction of a public interest test for transfers of large-scale landholdings; land ownership to be registered on the Land Register if the business is claiming support payments, and a requirement on owners of large-scale holdings to give prior notice to community bodies of their intention to sell.

Scottish Agricultural Bill

The new Agriculture Bill will underpin Scotland's Future Agriculture Support Regime from 2025 onwards and will focus on the Scottish Government's commitment to reducing agricultural emissions by 31% by 2032.

The Bill is expected to focus on protecting food and health quality, ensuring a fair income for farmers, supporting delivery of national climate change adaptation objectives, nature restoration and protecting biodiversity, fostering knowledge and innovation, and developing resilient and vibrant rural areas and island communities.

christine.beaton@sac.co.uk

2022 world prices remain high

The world saw a 48 Mt fall in the cereal harvest in 2022 due to Russia's war on Ukraine and adverse weather in the US and parts of Europe; while Canada, Australia and Russia saw bumper yields. The UK and Scotland saw a good harvest both in quality and high yields despite the hot dry weather which came late enough not to impact yields. Cereal stocks-to-use ratios fell further. According to USDA world grain output fell 47.8 Mt to 2,234 Mt; wheat output +1.2 Mt to 780.6 Mt, coarse grains output -49mt to 1,453 Mt. World grain demand fell 31.5 Mt. World grain stocks fell 16 Mt and stocks to use ratios fell to a 9 year low.

COCERAL estimates the EU+UK 2022 harvested grain crop at 285.5 Mt, down 24.3 Mt from the 309.8 Mt produced in 2021. Oilseed rape output was over 20 Mt, a recent high. In its first forecast for the 2023 cereal crop, a rise of 18.9 Mt to 304.4 Mt is seen.

For the 2022 UK harvest, winter cereal sowings rose, and wheat output lifted 11% to 15.5 Mt. This rise in UK wheat output was enough to move the UK to become a net wheat exporter. This has meant at times UK wheat prices have had to be export competitive but with a tight global situation overall price levels are higher than last year.

UK barley output rose 6% to 7.4 Mt due to high winter barley yields, while spring barley output fell 17% on the back of lower spring barley sowings. Barley's price discount to wheat in England remained quite low as in 2021 at £15-20/t in 2022.

In Scotland, 2021 cereal output rose to the highest level in 8 years at 3.1 Mt on yields that averaged 1t/ha higher at 7.6t/ha. Wheat output rose 10% and spring barley output rose 17%. Whisky grain demand has risen while the high price of imported maize has led distillers to switch to Scottish wheat. Malting barley premiums of £40/t at harvest were £25-£30/t higher than 2021.

Historic and future grain price summary

Sale period	Hvst '21	Hvst '22		Hvst '23
Date priced	**Dec-21**	**Dec-22**	***Change***	**Nov-23**
	(£/t)	***(£/t)***	***(£/t)***	***(£/t)***
Wheat	215	250	*+35*	245
Feed barley	200	220	*+20*	215
Malt. barley	280	260	*-20*	245
OSR	570	475	*-95*	485

Source: AHDB/SACC, Ex-farm Scot, * season av. Assuming 50% sold £20/futures pre harvest. #del.

2023 – more wheat, less malting barley

With global grain stocks-to-use tightening to their lowest level in 9 years by the end of 2022/23, the market will continue to closely monitor weather around the world. The Russian war on Ukraine shows no sign of ending and the impact on cereal production in Ukraine will only continue to be negative. At least for now grain shipments are continuing from Ukraine's ports so despite lower production supplies are reaching the world market.

In the UK, the initial AHDB early-bird survey sees 2022 winter cereal sowings higher; wheat +1%, winter barley +4%, oilseed rape + 14%, fallow +9%, but lower spring barley -6% and oats -4%. In Scotland, there was a big swing this autumn to wheat +8% and a fall in winter barley -13% and spring barley -4%. So far, crop condition is good across the UK. High maize prices and strong distilling premiums are encouraging more winter wheat. Spring barley area dropping is a potential issue for the malting and distilling sector if yields and malting quality do not rise as malting capacity has risen substantially in Scotland

Input costs rise: **-£** fertiliser and fuel prices remain high, so producers need to achieve high prices to recoup. With world oil reserves at their lowest level in 18 years, and a lack of investment in new production, high oil and energy prices look set to remain. As ever, buy fertiliser + sell grain = to lock in margin.

Global cereal S&D; **+£** Output < Demand, Stocks to use falls for 8th year in a row, forward grain prices are not high enough to compensate for high input costs. **-£** Economic growth under threat as high energy prices squeeze economies and China still grapples with Covid. The market remains vulnerable to weather conditions.

UK cereal S&D; **-£** UK a net wheat and cereal exporter in 2022, likely to continue in 2023 unless yields are poor.

+£/-£ UK 2023 early-bird area estimates – wheat up, spring barley area to decline.

Whisky: Future growth potential for whisky sales linked to world economic growth good but that is weakening.

- Buying today's inputs especially fertiliser by selling grain today helps cover high costs.
- Malting barley supply in Scotland to be squeezed by rise in winter wheat sowings

julian.bell@sac.co.uk, 07795 302264

2022 – High inputs vs high outputs?

2022 started well with a strong beef price around 420p/kg in January before dipping back in the spring with the usual increase in finished cattle availability. From March onwards the price continued to rise through the summer and peaking in November at 461.8p/kg for R4L steers.

The tightness in cattle availability throughout the year drove a lot of the price increases with demand being rather subdued.

One of the challenges currently facing the beef price is the consumers' rising cost of living which is impacting their shopping habits. With increases in beef prices on retailer shelves of around 10.5%, consumers have opted to trade down into these cheaper cuts. This has presented many processors with a carcase balance challenge with high stocks of steaks and roasting joints often being offered at reduced prices to move volume.

Beef producers, although welcoming the strong beef price this year, have been challenged with increases in input costs - mainly feed costs and the availability and cost of fertiliser. This has led, in particular, to many questioning the profitability of suckler cow enterprises

Strong cull cow trade

With the increase in demand for mince and a global shortage of manufacturing beef, the cull cow trade rocketed this year, peaking at around 410p/kg DW with cull cow live ring trade exceeding £2,000/hd for some of the heavier, beefier type of cow. The trade for these cows dipped back slightly as numbers available increased in the lead up to housing and scanning.

The strong cow trade and concerns over the profitability of the sector saw the numbers of cows slaughtered in Scotland rise considerably on the year. January – October 2022 saw 12% more cows slaughtered than the same period in 2021, with October 2022 alone seeing a 40% increase in the cow slaughter compared with 2021.

Combine this with an increase in the heifer kill in 2022, there will be a larger than anticipated contraction of the suckler herd in Scotland into 2023 and beyond. Store cattle continued to be a good trade in 2022 with prices at a similar level to 2021, with the exception of some of the lighter, longer keep cattle that appeared cheaper due to the increased costs associated to finish them.

2023 Beef Outlook

As consumers are faced with ongoing rises in the cost of living into 2023 and inflation continuing to be at a high level, it is unlikely that we will see a large rise in the demand for prime beef.

The demand for mince and cheaper cuts will remain strong and with it, the demand for cull cows is expected to be high in the new year. Cattle availability looks to remain tight as we go into 2023, however demand will dictate how much that will impact the beef price.

The recently released EU Agricultural Outlook 2022-2032 is estimating a drop in EU beef production of around 9% in the next decade with their suckler herd contracting by 6% in that time. However, they do expect global beef demand to continue to grow due to population growth and higher incomes in developing countries.

2022 has certainly brought challenges to the sector, but with that comes opportunities. These may be in the form of changes systems to be less reliant on inputs or changes in cattle numbers that work within your system.

If you are considering evaluating a change to your business there is funding up to £1,000 available through FAS Specialist Advice to look at your business in greater detail.

lesley.wylie@sac.co.uk, 01307 464033

Scotland prime cattle prices (p/kg dwt) (Source: drawn from AHDB and IAAS data)

Week Ending	R4L Steers (p/kg dwt)			-U4L Steers			Young Bulls -U3L		Cull cows	
		Change on week	Diff over North Eng.		Change on week	Diff over North Eng.		Diff over North Eng.	R4L	-O3L
26-Nov-22	**457.1**	-3.9	1.2	**455.6**	-4.4	3.1	447.5	-2.5	385.5	354.8
03-Dec-22	**457.8**	0.7	2.0	**455.3**	-0.3	-1.2	446.5	-3.7	383.1	349.0
10-Dec-22	**455.5**	-2.3	-0.5	**455.0**	-0.3	-0.3	442.7	-1.1	382.5	351.1

Milestones throughout 2022

2022 has seen some major steps to advance strategies for carbon reduction across the agricultural sector. While action may be behind where is needs to be to reach targets, important groundwork has been laid for action going forward, and Scotland remains ahead in ambition of other regions of the UK and other 'western' nations.

The launch of the Scottish Taskforce for Green and Sustainable Financial Services brought together financial experts to begin problem solving challenges around carbon finance, and scale up investment flows to maximise both public and private money.

A related network, the Scottish Nature Finance Pioneers (SNFP), has built a community of experts and practitioners in Scotland, providing crucial knowledge sharing of novel approaches to natural capital investment. Linked to the network, NatureScot, the Esmée Fairbairn Foundation and the National Lottery Heritage Fund launched the Investment Ready Nature Scotland (IRNS) Grant Scheme in August, to help organisations and partnerships develop projects in Scotland that use private investment and market-based mechanisms to help finance the restoration of the natural environment.

Much work continues behind the scenes at a policy level to design a new system of payments to support agricultural activities. The global energy & cost of living crises has moved goalposts and priorities for public spending drastically over the year.

Funding for the implementation and training around soil testing under Preparing for Sustainable Farming (PSF) begins to mainstream soil carbon monitoring and recording, and the scope for emerging competitiveness of Scotland in this area. As data & technology develops, this will be increasingly accessible layer of knowledge to farmers around land and asset management.

What's on the horizon?

The UK Farm and Soil Carbon Code (UKFSCC) has made significant progress throughout the year in advancing protocols that allow farmers to measure, record and verify (MRV) changes in soil carbon stock and GHG emissions as a result of adopting specific farming practices. In particular, a new framework is being created for carbon codes with Defra which will deal with the issue of variance in quality and specifics of requirements across carbon codes in practice in the UK and will be managed by an arms-length body.

Currently, the carbon codes verification process pays little attention to the details of MRV or specialist review for scientific rigour e.g. of soil testing methodologies. When implemented, this will be a major step forward in increasing the quality of carbon finance, a benefit to both potential sellers (farmers and land managers) and investors.

This sets the tone for the likely role of public funds in carbon credit generation & markets going forward. Governments are reluctant to play the role of a private market, compete with or undermine private investment; leveraging of private finance using a much smaller amount of public funds will be fundamental to achieve climate targets.

Policymakers are very aware of this, and to target public funding towards options/measures that the market won't (e.g. soil testing and reporting, infrastructure, knowledge/expertise), or providing a carbon price guarantee (a forwards floor price guarantee to de-risk and leverage private investment with a return on investment of ~30 years), and schemes are being developed with this in mind.

The new Scottish Government Agriculture Bill, due in 2023, expects to set out priorities for targeting public money for carbon and natural capital outcomes.

Planning the year ahead

There is a lot of cautious talk about carbon markets and finance currently, and for good reason. However, there are things that businesses might explore and consider adopting as the norm going forward.

- *While it is being funded, make sure you have a carbon baseline you can trust and explain which will provide solid evidence of any changes, required for future payments.*
- *If you are considering selling carbon credits at some point, think about how you might prove 'additionality' (i.e., that the action would not have been implemented without the carbon finance). There should be a paper trail ahead of implementation e.g., between the farm and advisor. Retrospective proof may not be valid.*
- *Start identifying potential interaction of carbon income streams with other forms of payments/ revenue e.g. biodiversity. 'Stacking' may be crucial for economic viability of measures on farm.*
- *Carbon markets bring together specialist areas of knowledge across agriculture, finance and carbon policy. Continually make the most of events and training opportunities, as the topic will evolve.*

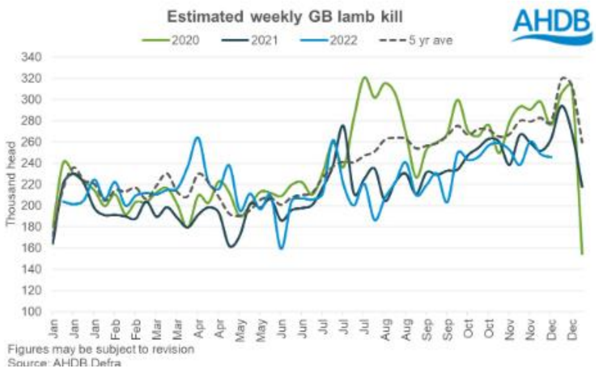
anna.sellars@sac.co.uk

Sheep

2022 Highlights

The domestic and global demand for sheep meat has been evident through 2022, combined with a tight global supply, which has sustained prices of all classes of sheep throughout the year. Following the conflict between Russia and Ukraine, the cost of inputs have soared on farms. With feed, fertiliser, fuel showing huge rises on the year, margins have tightened. We have also seen three prime ministers in the year, with changing policies and an increase in the cost of finance, which has been an additional hurdle to the sector.

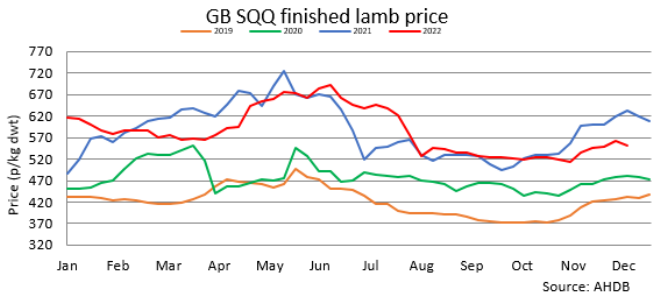
We have seen the contrast between the East and West. With the East having drought conditions in the summer which limited grass supply, while the West reported high levels of rainfall and an ocean of grass. The effect to the sheep on the East has largely shown poor growth rates in lambs and low condition in ewes. This has resulted in a lower than normal numbers being slaughtered in the second half of the year (2022 = blue on below chart).



The cull ewe trade has been exceptional, further showing the tight domestic and global supply of sheep meat.

The lamb trade opened the year exceptionally at 616.50p/kg SQQ DW, which exceeded the past three years. This tailed off throughout the spring has supply increased before taking another spike in the summer.

Unlike a typical year, this summer trade continued, with the seasonal slip being about a month behind normal due to both high demand for lamb, and the supply being tight with the drought. To date (16/12/22), we have not seen the high price we finished with in 2021, but we are still well above the 5-year average.



What does 2023 bring?

Given the high demand and tight supply of sheep meat across the globe, prices should be sustained going into the New Year. Consumption of sheep meat within the EU is set to increase by 0.20% per year until 2032 due partly to more people experimenting with different meats, migrating to the EU/UK from out with the EU and religion.

The much-awaited trade deals with Australia and New Zealand will come into play in the New Year. However, they will concentrate on markets with easier access e.g., Asia, this is especially true for New Zealand. With the lower production costs for the Australian and New Zealand lamb, the price gap will remain large compared to the EU lamb. As of the week ending 03/12/22, this price gap was €3.76/kg (NZ lamb = €4.76/kg DW and French lamb = €8.52/kg DW).

It is forecast that consumers will take more interest in the supply chain and how sustainably produced their food is. This offers a massive opportunity for Scotch lamb as we adapt farming systems to be less reliant on expensive inputs and maximise the assets of the land e.g., grassland production.

Kirsten Williams; 07798617293

Week ending	GB deadweight (p/kg) 16.5 – 21.5kg				Scottish auction (p/kg)				Ewes (£/hd)	
									Scottish	Eng&Wal
	R3L	Change on week	Diff over R2	Diff over R3H	Med.	Change on week	Diff over stan.	Diff over heavy	All	All
26-Nov-22	**553.0**	1.5	-2.0	-1.4	**244.10**	1.7	12.6	4.0	77.54	81.48
03-Dec-22	**565.0**	12.0	-5.5	-1.4	**247.90**	3.8	15.4	6.0	79.20	83.30
10-Dec-22	**556.7**	-8.3	-3.7	-0.2	**241.10**	-8.6	5.9	5.6	71.72	77.64

Deadweight prices may be provisional. Auction price reporting week is slightly different to the deadweight week. Source: AHDB and IAAS

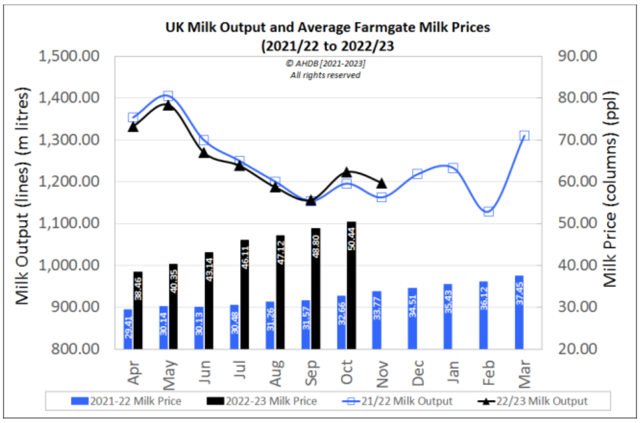
Milk

2022: A year of rocketing input costs and record highs farmgate milk price

- *Farm input costs have continued to increase throughout 2022.*
- *Farmgate milk prices have increased to a record high throughout the year to help cover rising input costs.*
- *A high farmgate milk price has produced a recovery to milk output, especially during the final quarter.*
- *Towards the end of 2022, dairy wholesale prices have weakened in response to increasing supply stock.*

2022 has certainly been a bit of a rollercoaster for the dairy sector, with input prices and farmgate milk prices experiencing unparalleled highs. Fertiliser prices remain high, feed prices continue to rise even further, and following the Russian invasion of Ukraine, costs for fuel, electricity, and power have shown little sign of easing. This all sounds like doom and gloom but 2022 has not been all bad! The negatives have been countered by some significant positives. During the 2022 calendar year, we have seen the average UK milk price increase by 42% from 35.43ppl to 50.44ppl for October 2022 (UK farmgate milk prices for November and December 2022 are not available from DEFRA at the time of writing). The high milk price has helped keep UK production on a broadly similar track to 2021 (see below). Nonetheless, dairy prices are subject to supply and demand, just like any other market. Whilst supplies for liquid milk are broadly in balance within the UK market, increasing stock of dairy commodities within the EU means that downward pressure on prices is looming.

AHDB milk production data shows that output for November 2022 is estimated at 1,197.84m litres (before butterfat adjustment) – an increase of 35.12m litres on a year-on-year basis. Cumulative UK production for the 2022/23 milk year to the end of November 2022 stands at 9,989.41m litres (before butterfat adjustment), which is 32.37m litres lower output compared with the same time last year. The UK average milk price for October 2022 is estimated at 50.44ppl, an increase of 1.64ppl from the previous month (48.80ppl) and a year-on-year increase of 17.78ppl from October 2021.



2023: Downward pressure on prices predicted for the New Year

Towards the end of 2022, dairy wholesale prices started to show signs of weakening and this is clear to see with the reduction to the value of AMPE from 51.27ppl for October 2022 down to 44.69ppl for November 2022. In 2023, high food price inflation together with rising interest rates are likely to result in a further weakening of dairy markets as growing numbers of consumers try to be savvier with their weekly shopping budgets in in response to reduced purchasing power. Although some growth is predicted for global milk output in 2023, growth is likely to be modest if farm input costs remain at their current levels. Production growth in 2023 may also be limited by price reductions, depending upon the extent of any downturn in the market.

Some milk buyers have already started to react to changes in dairy markets. South of the border, Meadow Foods, Freshways, and Pensworth Dairy have all announced price cuts for January 2023. Meanwhile, in Scotland, Müller and First Milk have both confirmed a hold on prices for January.

To date, announcements for January 2023 include:

- Müller Direct – Price hold confirmed for January.
- Müller organic – As above, a price hold has been confirmed for January 2023. The organic farmgate milk price holds at 56.00ppl for January 2023.
- First Milk – FM has confirmed a hold on prices from December 2022 into January 2023.
- Fresh Milk Company – No change confirmed as yet.

Annual average milk price estimates for January 2023 (ppl)	
Milk Prices – Scotland	**Standard Ltr***
Lactalis / Fresh Milk Co. (No profile or seasonality) [1]	48.21
First Milk Liquid [1, 2]	48.02
First Milk Manufacturing *(4.2% Butterfat & 3.4% Protein)* [2]	49.69
Müller - Müller Direct - Scotland [1, 3]	47.75

1 *Liquid standard litre – annual av. milk price based on supplying 1m litres at 4.0% butterfat, 3.3% protein, bactoscan = 30, SCC = 200 unless stated otherwise.*

2 *The FM member premium is set to remain at 0.50ppl from April 2022.*

3 *No monthly supplementary payment included in the price estimate. Includes 1.00ppl Müller Direct Premium and additional 0.25ppl haulage charge for Scottish suppliers.*

UK dairy commodity prices (£/ tonne)	Nov 2022	Oct 2022	May 2022
Butter	5,280	5,860	5,890
SMP	2,610	2,980	3,310
Bulk Cream	2,357	2,807	2,579
Mild Cheddar	4,760	4,860	4,650
UK milk price equivalents (ppl)	**Nov 2022**	**Oct 2022**	**May 2022**
AMPE (2021)	44.69	51.27	55.10
MCVE (2021)	52.29	53.95	53.14

Dates for the Diary

- Semex Conference: 15th – 17th January 2023

www.semexmarketing.co.uk/conference-2023-new

alastair.beattie@sac.co.uk, 07771 797 491

Introduction

Prospects for Scottish agriculture in 2023 will continue to be heavily shaped by global forces. While the chief forces to be aware of, coupled with how the main types of farming practised across Scotland might be affected are given below; as ever, it is how businesses adapt to changing circumstances that will be key to individual success.

Ukraine war pivotal

The conflict in Ukraine will continue to hit western European agriculture badly because 40-50% of EU gas is imported, mainly from Russia. Fortunately, gas storage had been successfully topped up in 2022 and despite the recent cold snap, no power cuts are expected for the 2022/23 winter. Energy, however, is extremely expensive, especially fertiliser and electricity. Topping up European gas storage in 2023 will remain very expensive as no gas will come from Russia. Energy forecasters do not expect new global gas production to come on-line until 2024.

The recent easing in oil prices has sparked some optimism for lower diesel prices. However, much will depend on how the west's recently implemented oil price cap on Russian production works. The scheme aims to curtail Russian income from oil sales rather than interfere with global supply and prices.

Cost of living crisis to continue

Stagflation is the term given to both inflation and recession hitting the economy at the same time. Neither economic condition is good alone, but together normally mean a big squeeze on household incomes and hence consumer demand. As people must eat and drink, demand for farm produced food products is less badly affected than for most other sectors of the economy. Nevertheless, recent retail surveys reveal how consumers are responding, switching to cheaper meats, eating out less, reduced interest in paying premium prices for products with health and environmental attributes.

In short, with continued food price inflation forecast, albeit at a declining level, cost will be the main driver of food demand, which will feed through to farmgate prices. For farmgate prices are not generally set by cost-plus systems: egg producers certainly found that out in 2022.

Higher interest rates will further dampen consumer spending. Though the recent Bank of England economic forecast points to inflation returning to target in a couple of years' time (from the current 10.7% down to 2%); another lift in the base rate to 3.5% was recently announced. Further increases in the base rate are anticipated: how these impact economic growth and jobs is the big concern.

Trade deals and exchange rates

A further consideration in setting the base rate, is the exchange rate, which has big implications for trade. While a weak pound helps agriculture by making exports more competitive and imports less so, it also pushes up the cost of farm inputs, much of which come from abroad. Further, as most global commodity markets are priced in US dollars, the strong dollar is exacerbating input costs like fuel and fertiliser. The good news is that the latest forecast from the Federal Reserve, the US Central Bank, is for inflation to fall quicker than previously expected so although further rate rises are expected, the peak interest rate should be less than previously forecast. Notably sterling has recovered sharply against the US dollar in recent months.

Trade in the coming year will also be influenced by how several recent trade deals play out. Limited mention of the Northern Ireland protocol of late suggests that negotiations are currently intense. If an updated protocol can be agreed, it could improve the overall UK-EU trade deal by reducing paperwork. A vet deal to eliminate most of the sanitary and phyto -sanitary controls may be key to an agreement. Even so, it is hard to grasp why the UK has implemented few checks on imported food products to date.

As for the sterling-euro exchange rate, at the time of writing, it is almost exactly where it was five years ago at 87p/€. For if there are considerable clouds over the UK outlook, the half-baked mechanism to manage the euro could well come under strain again in 2023, weakening the euro.

By the end of 2023, the first shipments of meat from Australia under the new UK-AUS free trade deal should have landed. Ratification is expected soon by the Australian parliament. Here, the deal is already ratified (by default), but still needs passing into law. It will be interesting to see how the Australians target the big UK market. On a more positive note, one factor that still offers some protection from imports from New Zealand and, potentially, Australia is the continued unreliability of chilled container freight – a legacy from Covid.

And look out for the UK joining the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in 2023 to get better access to the region of the world forecast to grow most in the coming decades – Asia. The Chinese also have their application in.

(cont.)

Covid and animal disease

While the direct impact of covid is receding here, China's Zero Covid policy is badly disrupting the Chinese economy. As a massive importer of food and fuel and exporter of agrochemical products and fertiliser, what happens in China has global impact. The forced lifting of lockdowns could badly affect China given the low proportion of elderly Chinese fully vaccinated. Growing geopolitical tensions add further uncertainties, a reason why the Aussies and Kiwis were pleased to sign trade deals with the UK.

Here, bird flu (which also originated in China) is the disease most likely to impact egg and poultry production in the months ahead especially as it is now rife in the wild bird population.

Farm policy status quo in Scotland

Agricultural support for Scottish farmers will change little in 2023, which given the considerable volatility/uncertainty affecting prices and costs, is a blessing.

By comparison, English farmers 2023 area payments will be 35-55% less than their 2020 payments depending on payment band; with the apparently 'generous' capital grants for updating slurry storage and improving productivity being funded from reallocated area payment cuts. However, given concerns about the negative impact on food production of fully removing area payments, plus the difficulty of designing workable environmental schemes, could Defra volte-face and keep some area payments long term?

The new CAP programmes start in EU countries in January 2023. Again, there is a clear funding strategy of "robbing Peter to pay Paul". All member states have been forced to allocate a quarter of area payments to eco-schemes though they have been given considerable scope to customise such schemes to their own national circumstances.

Scottish farmers also appear under less pressure to reduce greenhouse gas emissions than many other countries in 2023. Scotland is adopting a nudge policy to encourage farmers to do the right thing to cut emissions through the likes of the National Test Programme. But Dutch dairy farming will be cut by buying out some farms, the Irish are considering similar action for its sucker herd. While Kiwi farmers are protesting loudly about proposals to tax them from 2025 to help meet their national climate change targets.

Impact on main Scottish farm types

Hill farms less exposed to input cost inflation

With hill farm livestock sales typically concentrated in the autumn; the prices of store lambs, breeding sheep and weaned calves will be set by the trade for finished lambs and cattle.

Cost of living pressures both here and Europe point to some softening of prices. Excellent growing conditions in the summer meant that any cutbacks in fertiliser did not show up in pasture and silage yields. Mother nature may not be so helpful this year.

Pressure on upland cow numbers

Upland farmers with cattle will be hoping that the spring yearling sales set a positive tone. Certainly, cattle supply globally is predicted to be tighter. Excellent demand for mince beef is encouraging farmers to cull any passengers especially as silage has become a very expensive feed given the cost of fertiliser and contracting. How upland farmers rebalance their farms may become clearer in 2023.

Only one direction for milk prices

Most dairy experts are pencilling in a milk price drop. Fortunately, most milk contracts have reached levels where some, limited, reversal will be manageable. As dairy farming is very exposed to input cost inflation, any softening in feed costs should lower production. Good use of slurry and generally high soil indices also offer savings in the fertiliser bill. Notably, given all the talk of conditions being attached to future support in Scotland, dairy farmers already operate to conditions (e.g., non-euthanising calves) set by their milk buyer.

Crop farmers holding their breath

Cereal farmers had a pretty good 2022 crop year thanks to favourable 2021 input prices and strong prices. With the 2023 crop growing on high costs, growers are keeping a close eye on how developments in Ukraine affect the global grain market. Many farmers have already modified crop rotations to reduce costs, some are also experimenting with tie-ups with livestock farmers to improve returns and build soil carbon.

Sympathy due to pig, poultry and fruit farmers

Finally, spare a thought for the sectors that had a terrible 2022. Intensive livestock profitability will improve if grain prices ease lower and maybe egg producers will get a better deal with supermarkets. But resolving labour shortages may remain difficult.

Kev Bevan, 07368 825877

Financial Matters

2022 - A year of uncertainty

2022 has been a tumultuous political and financial year for the UK, with three Prime Ministers and four Chancellors within the calendar year; each bringing their own unique impact on the UK economy.

The pandemic has left a weaker economy and the war in Ukraine has significantly impacted energy prices. With inflation peaking at 11.1% in the 12 months to October 2022, prices have risen significantly.

The agricultural price index for input costs increased by 28.3% in the year to October 2022, with agricultural outputs increasing by 22.3%. Key drivers of costs were fertiliser (↑83%), energy (↑52%) and feedstuffs (↑ over 30%). The increase in output sale prices is more sector dependent; milk has increased by 54% and cereal crops are up approximately 40%, but potatoes and sheep have remained steady with poultry slightly decreasing.

Changes in fiscal policy

Following the September 'mini-budget' and its subsequent fallout, the UK Government have now taken a more conservative approach to taxation; as seen in the UK November Autumn Statement.

Key changes for agriculture include retaining the Annual Investment Allowance at £1m on a permanent basis. This allows investment in plant and machinery when best suited to business needs, rather than just for tax purposes.

Corporation Tax will increase to a main rate of 25% from April 2023 for profits of £250k and over. Profits of up to £50k will still be taxed at 19%, those between these figures are subject to a tapered rate.

Along with the personal allowance of £12,570 remaining frozen until 2028, Scottish Government announced in their 15 December budget statement that the starter, basic and intermediate rate bands of Income Tax would remain unchanged, rather than rising with inflation like last year. As inflationary pressures drive up wages, this leaves individuals paying more tax for the same jobs. The higher and top tax rates will rise by 1%, to 42% and 47% respectively. Earning £35k, this equates to a difference of approximately £300. On £50k, this rises to approximately £2k difference. All individuals earning over £14,733 pay more Income Tax than those in England. The top Scottish rate tax threshold will be reduced from £150,000 to £125,140, in line with the rest of the UK.

Other changes of note include halving the current Capital Gains Tax allowance of £12.3k and dividend allowance of £2k in April 2023 and again in April 2024. This will result in allowances of £3k and £0.5k from April 2024. Finally, the Scottish Government announced the Additional Dwelling Supplement within LBTT will rise from 4% to 6%.

Within the Scottish Government's budget for agriculture, funding for Pillar 1 and LFASS remains the same for 2023/24. Funding has also been maintained for Agri environmental measures, with AECS funding rounds currently in place until 2024.

The year to come

On 15 December, the Bank of England announced an increase to 3.5% in the base interest rate. Many analysts predict rates will rise to approximately 4.5% or 5% in 2023, before settling around 3% in the medium term. This is a tool that is used to help curb the rates of inflation, however a return to the target of 2% inflation is not expected until 2024.

This is a sentiment being echoed globally with the US Federal Reserve and European Central Bank each raising interest rates by 0.5% in December.

It is anticipated that inflation has now peaked and will begin to fall gradually in spring, with many analysts predicting a rate of around 3% by the end of 2023.

andrew.coalter@sac.co.uk, 07721 473 566

Key economic data

General Indicators	
Base interest rate	3.5% (3% Nov 22)
ECB interest rate	2.0% (1.5% Nov 22)
UK (CPI) inflation rate	10.7% (target 2%)
UK GDP growth rate	-0.2% (Q3 '22)
FTSE 100	7,435 (21 Dec 22)

Price indices for December 2022 (Defra 2015 = 100)			
Output Prices		Input Prices	
Wheat	230.8	Seeds (all)	123.8
Barley	224.9	Energy	213.4
Oats	203.3	Fertiliser	299.0
Potatoes	138.2	Agro chemicals (all)	161.8
Cattle and Calves	132.6	Feedstuffs	180.7
Pigs	152.3	Machinery R&M	127.1
Sheep and Lambs	134.0	Building R&M	159.8
Milk	209.5	Veterinary services	118.2

This publication is funded by the Scottish Government as part of the SRDP Farm Advisory Service