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Cairngorm Monitor Farm

**A & J Adams
Eastfield Farm
Ballater
Aberdeenshire**

**Report on Meeting held Tuesday 4th March 2008
Profitable Conservation and Analyzing your Accounts**

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SCOTTISH EXECUTIVE

TOP TIPS FROM THIS MEETING

1. The new SRDP will provide good opportunities for farmers and landowners to take advantage of agri-environment schemes. You need to think about what you want to do to protect and enhance the environmental aspects of the farm. There is a new on-line application process. Help is available from a variety of sources.
2. The use and analysis of farm accounts is a powerful tool to improve business performance. Many businesses are not making enough use of their accounts. Training is available if required.
3. There is tremendous value in converting farm accounts into a 'gross output' format and calculating key costs as a % of the total gross output. The 'rules of thumb' for gross output analysis helps identify potential weaknesses for further investigation.

The meeting started at Eastfield Farm, then moved on to the Glenaden Hotel, Ballater. Lunch was kindly sponsored by the Clydesdale Bank PLC.

Meeting Aim: Introduction to environmental schemes in new SRDP
How to analyse your farm accounts

Programme;

- Eastfield Farm, update on farm activities
- Introduction to SRDP and environment schemes
- Glenaden Hotel, Ballater. Lunch 12.30
- How a bank assesses a farm business
- 'Idiots guide to analysing your farm accounts'

1. Farm Update (Monitor Farmer, Alan Adams)

- PD 20 heifers; 18 in-calf. 2 not in calf sold average £700.
- Half of heifers have now calved
- Annual test of herd for Johne's disease - had 16 reactors (9 reactors last year). Of which 12 were first calvers, three 2nd calvers, and one 3rd calver. These will be culled when calves weaned.
- Will be selling 21 forward stores on Friday (7th March) at Thainstone, expect good trade
- Bought new AA Bull at Perth Bull sales (£3,000 gns)
- Got 29t of Nitram home, cost £275/t

- Ploughing up an extra 55ac of grass - will have total of 200ac sp barley this year
- Ley fields will be down to feed barley - variety 'Wagon'. Other fields down to malting barley – 'Oxbridge'.
- Soil analysis done; most fields okay pH, but 2 fields low pH 5.2 and 5.3.
- 200t lime applied to stubble / grass prior to ploughing. Will use Calciprill on fields with low pH – calcium carbonate more available first year.
- Dressed own barley for seed (cost £80/t) and bought some new seed £440/t
- Will have a pit of silage left unopened.
- Currently use Fibrephos (6cwts/ac @ 0.16.16) every 3 years for basal P and K for cereals.
- Note: A 2tonne/ac barley crop will remove 50 units of P and K per acre so P & K a bit short although fields get FYM.

2. The New SRDP and opportunities for environmental schemes. (Alison Espie)

Alison Espie works as an independent conservation adviser. She has extensive experience in Deeside and supported the Monitor Farm's conservation schemes.

This was an introductory session to conservation opportunities under the new Scottish Rural Development Programme (SRDP)

Summary of main points:

SRDP Funding 2007-13, total value £1.6bn

Tier 1	SFP and GEAC
Tier 2	Land Management Options (LMO) similar to previous LMC's although some options removed
Tier 3	Rural Development Contracts (RDC). Will replace all existing schemes e.g. RSS, CPS, etc . Is competitive

RDC's

Outcome lead, Government want to see results.

Key outcomes:

1. Business Development
2. Biodiversity / Environment
3. Water
4. Climate Change

5. Rural Communities

Agri-environment schemes will have biggest budget within the RDC's
Regional boundaries - 11 RPAC's in Scotland although National RPAC has budget control

Starting point – what do I want to do on the farm?

There are 35 packages with a total of 115 options.

The new scheme will have an improved application process (unlike previous RSS debacle)

Application process –

- ❑ All applications must be on-line so farmers may need support to complete
- ❑ Scope proposal against priorities and options
- ❑ Need to commit an outline proposal (statement of intent) only 1-page
- ❑ Assessed by Government staff who will allocate a Case Officer (~26 in Grampian)
- ❑ At early stage will get either 'red' or 'amber' light and recommendations how to modify if required
- ❑ Can modify until 'commit' plan
- ❑ Assessed by RPAC who will meet 3 times/year to decide if applications approved

Assessment criteria: - fit regional priority, value for money, and management of risk.

Still waiting the final detail for all the schemes. Expect Forestry and organic schemes to continue.

Any existing environmental schemes (e.g. RSS) will continue to end of their life.

Dept staff will have a more advisory / supportive role

Expect budget to be circa £3M per year.

Capital grant rates: LFA 50% and Non-LFA 40%.

Following the update on SRDP details, the group took a walk to look at one of Eastfield's RSS
- fencing of a birch wood to prevent cattle damaging the woodland and re-generated plants.

GLENADEN HOTEL, BALLATER

3. Assessing a farm business – Banker's perspective (Mike Singer)

Following lunch, sponsored by Clydesdale Bank, Mike Singer (Agricultural Manager), and William Wyness (Business Development), Clydesdale Bank, gave a brief presentation on how the Bank assesses a farm business.

- Short introduction given of how the Bank transfer information from the annual Financial Accounts to it's own Progressive Analysis of Farmers Financial Accounts (PAFFA).
- PAFFA gives Balance sheet data, Gross Output data and Profitability data covering a 5 year period. This is useful for historic trend analysis.

- PAFFA also produces a Cash Flow report showing surplus / deficit for that year.
- Explanation of how ratio data is then transferred from PAFFA to a Simplified Forward Budget, (SFB) Tool. This tool allows the Bank, in conjunction with data provided by the customer, to forecast cash surplus / deficit, using Projected Gross Output, historic Profit ratio, Depreciation, Finance costs etc. This is very useful when considering any Capex on the Farm or indeed further expansion as Output's can be adjusted etc to confirm ongoing business viability.
- An example of the above PAFFA and SFB was issued to all present based on a 650 acre Farm carrying 130 cows and 250 breeding sheep.
- William Wyness followed with a brief summary of his role with the Bank, which is to bring new business to the bank. He works mostly in Agriculture, but also gets involved in a wide variety of other business.
- A Q & A session followed based on the above.

4. Analysing your farm accounts (Peter Cook)

This was a brief review session for farmers looking to analyse their farm accounts. To illustrate the layout of accounts a summary of the Monitor Farm's were distributed. See **Appendix 1** for handout circulated at the meeting.

Summary of main points:

The Accounting Model was explained. Cashflow is simply actual cash movements – cash in minus cash out. However a business does not just trade over 12 mths and stop, so have to make adjustments to cashflow for outstanding debtors and creditors, and assets created still to sale (valuation changes). Also capital expenditure is not used up in one year, spread over investment's life.

So profit is cash adjusted for

- debtors (folk owe you money)
- creditors (you owe)
- valuation changes
- Depreciation (capital exp)

Balance Sheet shows estimate of your wealth (Net Worth) at one point in time. Lists all the assets and liabilities in a business, in order of liquidity. Shows the 'net worth' – the wealth of the business. Aim is to increase the new worth. Must check if valuations are correct.

Farm Business Analysis

Summary:

- In general, businesses not making enough use of their accounts to improve the management and performance of their business
- Tax accounts are different from management accounts so need to be amended
- Convert into the standard format of 'gross output' and carry out gross output analysis of key costs. Have developed good thumbs of rules for main costs – see handout
- Don't just look at one year, need to consider trends over 3 – 5 years.
- Consider valuations, are they realistic?

5. Review of Project's progress to date

Since this was the last meeting of the Project's first winter the facilitators were looking for feedback on the Project's progress to date. Points raised by the Group included:

- The meetings have covered a good range of topics.
- Everyone agreed meetings had been relevant and interesting
- Took time to get to know farm, its system, and strengths/weaknesses
- The timing of meetings from 11 – 3.00pm was thought to be good. Was long enough and allowed time over short lunch for networking
- Reports from the meetings were welcomed and useful. One criticism is that they should be out earlier, within a week of the meeting.

APPENDIX 1

Monitor Farm Meeting (March 2008)

FARM BUSINESS ANALYSIS

1. The need for analysis

If a farm business is to be managed efficiently - achieve its potential - the farmer/manager must be provided with information on the use that is currently being made of its resources; ie land, labour and capital.

To assess the farm's performance you must try and pinpoint the good and bad aspects of the business, before taking steps to bring about any alteration in the business which will help achieve your objectives.

The following stages provide an approach to analysing a farm business. The main value is to develop a better understanding of the business and how it can be improved.

It is rarely a process that provides clear sharp answers but one which can establish a framework to allow you to start to make an overall assessment and provide a 'lead in' to handling problems. In addition to making an assessment of the most recent year, you should look at the trend over a number of years, partly to ascertain whether there are consistent trends and partly to determine whether or not the current year is exceptional.

So need to look at the trend over 3 to 5 years.

There are 3 basic methods for analysing the accounts of farm business

1. Review the P&L and Balance Sheet
2. Gross Output Analysis
3. Comparative Whole Farm Accounts

- *Generally, farmers do not make enough use of their accounts to improve business performance*
- *Remember, need to amend tax accounts into standard format (management accounts) for ease of analysis.*

ANALYSING FARM ACCOUNTS

KEY QUESTIONS

Is the profit adequate?

- Living expenses, Debt repayment
 - New Investment Margin for risk
 - Adequate reward for risk and management
1. How does the farm's total output look; the output per acre (ha)
 2. Is there a profit – if not, potential output/input problem.
 3. Is profit greater or less than personal drawings – if greater, then there is growth arising from the production process.
 4. If there is Net Worth growth – is it being used to reduce liabilities to others or to increase assets? If the latter then what assets are increasing (eg long term in say land or more short term productive livestock).
 5. If there is no Net Worth growth but business size is increasing then the funds are coming from increased borrowings with its implications for future interest charges.
 6. Do personal drawings use up all or more than the profit, if so why. Eg are funds being withdrawn for some other business opportunity or for consumption. What are the likely implications?
 7. Is extra personal capital being introduced to maintain the level of Net Worth?
 8. What is the 'percent owned' as an indicator of security, credit worthiness, and vulnerability of the business to interest charges.
 9. What is happening to individual items in the Balance Sheet eg is investment in equipment being run down or increased, are debtors buildings up?
 10. What is the 'rental equivalent' for rent + interest per acre (ha)? Is that serviceable?
 11. How do trends in Net Worth and assets compare with inflation rates over a time period?
 12. What returns on capital are being obtained and how do these compare with potential returns in other business opportunities and in secure investments eg building societies?
 13. How vulnerable might the business be to changes in interest rates, family circumstances, etc.

GROSS OUTPUT ANALYSIS

Gross Output Analysis, is a simple technique where a farm business's 'Profit and Loss' account can be analysed and compared to the norms expected for a mixed arable/livestock farm. All the costs are calculated as a % of the total Gross Output (G.O.). This is a simple quick guide to examine the cost structures in a business.

The information is based on experience of the normal cost/output relationships in many farm businesses, it is really a form of simplified comparative analysis.

	<u>% of G.O. (norms)</u>
Total Output	100
Variable Costs	30-40
Gross Margin	60-70
Labour	15-18
Power	15-18
Overheads	4-6
Fixed Charges (Rent & Interest)	15
Net Profit	15

Adjustments would have to be made to the 'norms' if the farm includes an intensive livestock enterprise.

The Gross Margin as a percentage of Gross Output provides an indication of the technical efficiency of the farming activities. If it is under 60% of the Gross Output for the arable, beef and sheep farm, some thinking on efficiency aspects should take place. The all-arable farm may be up to 70% while the specialist intensive livestock unit or dairy farm may be down to 55%.

Labour and Mechanisation costs (covering machinery depreciation, repairs, fuel and electricity, and contract work) should be within the 30-35% range. If they are beyond this then the organisational aspects of the business should be examined in detail (eg machinery and labour costs).

Gross Profit (ie profit before Fixed Charges), should be at least 30% of the Gross Output to meet Fixed Charges and other calls on profit (eg Private Drawings).

Fixed Charges (rent, rates and interest) should normally be under 15% and definitely not over 20% of Gross Output even for the most efficient operators. If they exceed these levels the farm is probably over-borrowed.

Net Profit should hopefully be 10 -15% of Gross Output.

NOTE: Gross Output = (Sales of Crops and Livestock plus Closing Valuation of crops (harvested and growing), home-grown fodder and livestock minus (Opening Valuations of crops, fodder and livestock plus Livestock Purchases).

COMPARATIVE WHOLE-FARM ANALYSIS

There is a statutory requirement for member countries within the EU to provide for the European Commission's data for FADN. This data is normally gathered by individual countries through a Farm Account Scheme (FAS). Here a representative sample of farm businesses is monitored to produce standard physical and financial data. In Scotland, there are approx. 600 farms contributing to the FAS across 9 different farm types. The principal aim of the FAS is to provide information on farm performance so as Government & EU can assess the impact of agricultural policy decisions. However, the information gathered can also be used by the industry, through a variety of ways, to improve business performance at the micro level.

The farm accounts, with supplementary physical information (if available) are compared with:

- i) Previous results of the same farm.
- ii) results from other farms in the same area and of a similar type.

For comparative purposes all farms are treated as though they were tenanted, pay for all manual labour, including family labour and have no charges for interest (ie they are all self-financing).

The analysis involves assessing and comparing levels of farm output, variable costs, gross margin, fixed costs and "profit" etc with similar farms. "Profit" in this type of analysis is adjusted to Management and Investment Income (MII).

Sources of Benchmarking data for comparisons

1. Government

On DEFRA web site on-line. (www.farmbusinesssurvey.co.uk/benchmarking/Default.aspx/)

Country: Scotland

Farm Type: choose drop down menu (General Cropping)

Farm Size: Choose small, med, large

Scottish Government Economic Report on Scottish Agric 2007.
available either to purchase or on-line

2 SAC Farm Management Handbook

3. Some Banks and Accountants may do for clients