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RURAL BULLETIN

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Welcome to this latest issue of the Knight Frank Rural Bulletin

Does the new decade herald a new attitude to farming and the countryside from the government? For once the initiatives coming out of Whitehall seem largely positive. So far this year we have seen a new twenty-year vision for food and farming that pushes agriculture up the political agenda, while the announcement of a supermarket ombudsman suggests that the growing power of the retailers has at last been recognised. Even the latest reform of the planning system looks as if it could be helpful to rural businesses.

A looming general election might partly answer the question and talk is always cheap, but the real challenges for agriculture – volatile commodity and input prices and an increasing environmental burden, not to mention the imminent reform of the Common Agricultural Policy – will remain whoever wins power. It looks set to be another interesting decade. If Knight Frank can be of help in any way you can find contacts for our wide variety of rural service lines on the final page of this bulletin.

Headlines

- **Farmland values end decade on high**
- **Commodities – a decade of volatility**
- **Government launches plan for farming**
- **Prime property recovery continues**
- **Planning boost for rural businesses**
- **Private water supply regulations**
- **Supermarket ombudsman gets the go ahead**
- **CAP reform process starts**

FARMLAND MARKET – LAND VALUES END DECADE ON RECORD HIGH

Farmland values recovered quickly from the drops experienced during the credit crunch and were back at record highs by the end of 2009. Compared with other property sectors and the FTSE 100 index, farmland was clearly the star performer of the last decade.

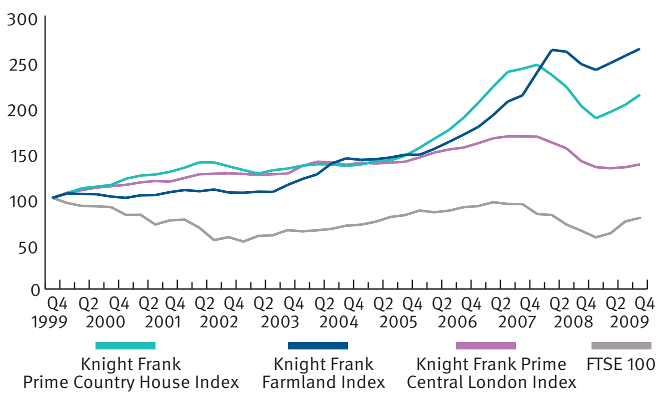
According to the Knight Frank Farmland Index, the average value of English farmland has increased by at least 3% in each of the past three quarters and rose by a total of almost 7% in 2009. The index is now sitting at £5,123/acre, fractionally above the £5,100/acre it reached in the second quarter of 2008.

The index, of course, covers a wide variety of farmland types and locations. Land of the right quality and in the right place continues to attract competitive bidding and can make upwards of £7,000/acre. If the imbalance of supply and demand that has helped sustain values continues we expect the price of farmland to continue rising through the new decade.

Fewer than 150,000 acres of farmland were advertised publicly last year, a drop of 30% compared with 2008 and significantly down on availability at the beginning of the last decade. There are few signs that this trend will change to any extent in the near future unless the next government decides to increase the tax burden on farmland ownership.

Demand for farmland remains strong from farmers looking to expand their businesses and investors attracted by the potential of strong capital growth and long-term stability. Lifestyle buyers looking for attractive residential farms are still in the market, but not at the levels seen at the height of the property boom. This should change, however, as memories of the credit crunch fade.

Farmland performance versus other asset classes
(Q4 1999 to Q4 2009)



Source: Knight Frank Residential Research

COMMODITIES – A DECADE OF VOLATILITY

It is not an understatement to say that commodity markets have been on a rollercoaster ride over the past decade. As the graph below shows, arable farmers saw the price of their wheat crops virtually double in value in a season before halving just as quickly. Livestock prices would show a similar, although slightly less pronounced, pattern.

For much of the past 10 years subsidy payments have kept the UK's farming industry in profit. Even during the good years input prices, as illustrated by the price of oil on the graph, have tended to increase in parallel with commodity prices, eating up much of the potential extra profit. According to farm business consultant Andersons, the total income from farming (TIFF) was only positive without the help of subsidies in two years during the decade.

The livestock sector has been hit particularly hard. UK breeding sheep numbers have dropped by about 25% to 15m, while the beef herd has fallen by 900,000 head. The number of English dairy holdings has dwindled by over 40% to well under 10,000 and UK milk output dropped by a billion litres in the past five years.

Of course, every industry must rationalise to survive, but many livestock businesses are still worryingly not showing a real return on investment even though prices are relatively healthy at the moment. According to the English Beef and Lamb Executive, a fully costed sheep business needs to sell its lambs consistently for 400p/kg/dw just to cover costs. Last year, when the weak pound helped push up prices, only the top third of beef finishers showed a positive margin, says Andersons.

The good news for 2010 is that the cost of some major inputs such as fertiliser and finance has fallen over the past 12 months and the cost of production for this year's wheat harvest is forecast to dip from £110-£145/t to £100-£135/t. Sadly, there is little to suggest wheat prices will move much higher than £110/t this year meaning most arable farmers will once again be relying on subsidy payments for their profits.

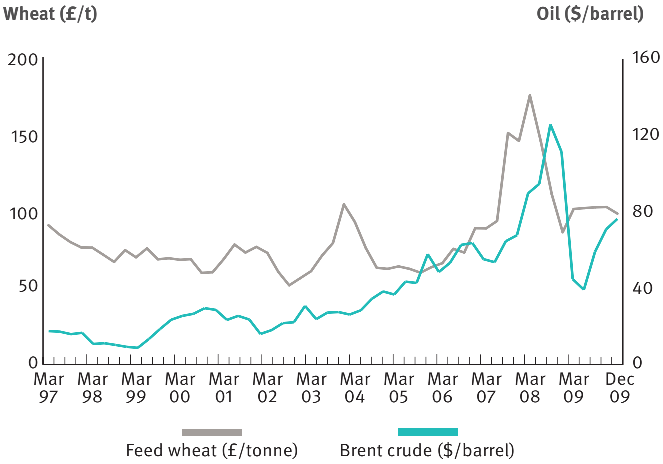
Looking further ahead, we can be cautiously optimistic about the rest of the decade. Food and agribusiness specialist Rabobank believes the dairy sector is poised for a revival and a growing global population will need to be fed somehow. But all agree that commodity price volatility is set to remain. Those who can factor into their businesses will be best placed to survive.

Agricultural price changes 2008-2009

Commodity prices	Dec 2009	Sep 2009	Dec 2008	Quarterly change (%)	Annual change (%)
Feed wheat (£/t ex-farm)	102	91	90	12%	13%
Oilseed Rape (£/t ex-farm)	241	218	231	11%	4%
Cattle (R4L steers p/kg dw)	288	285	278	1%	4%
Sheep (R3L lambs p/kg dw)	383	323	292	19%	31%
Pigs (DAPP p/kg dw GB av)	138	150	131	-8%	5%
Milk (UK p/litre)	24.4*	24.1	26.4	1%	-8%
Skimmed milk powder (£/t)	1750	1550	1750	13%	0%
Input prices					
Red Diesel (p/litre)	45	43	41	5%	10%
Oil ($/barrel OPEC index)	74	67	39	10%	90%
Fertiliser (£/t AN 34.5%)	188	182	381	3%	-51%
Soyameal feed (Argentine £/t)	291	n/a	n/a	n/a	n/a
Economic indicators					
Interest rates (B of E base %)	0.5	0.5	2.0	0%	-75%
Inflation (CPI)	2.9	1.1	1.0	164%	190%
£:€ rate	1.22	1.10	1.46	11%	-16%
£:$ rate	1.63	1.60	1.55	2%	5%

*October

Wheat prices v oil



Sources: Farmers Weekly, DairyCo, DEFRA, Knight Frank Research, HGCA, EIA

SUPERMARKET OMBUDSMAN ON THE WAY

The government has agreed to introduce a supermarket ombudsman to monitor the relationship between retailers and their suppliers and enforce the Groceries Supply Code of Practice that will take effect on 4 February, 2010. A consultation has been launched to decide how the code should be enforced.

Such a move has long been advocated by the Country Land and Business Association (CLA) and the National Farmers Union (NFU) who say that farmers and suppliers are not always treated fairly by the supermarkets. But the British Retail Consortium claims it will add cost to the food chain and is not necessary because most of the supermarket suppliers are large food businesses that can stand up for themselves. It said there was already a supplier code overseen by the Office of Fair Trading that offered the right to independent arbitration.

GOVERNMENT FINALLY COMES UP WITH PLAN FOR FARMING

Agriculture hit the headlines in the New Year as the government launched the UK's first major food and farming strategy in over 50 years at the Oxford Farming Conference.

Food 2030, which has six main aims, has been generally welcomed by the agricultural industry for its recognition, at long last, that farming plays a vital role in the UK economy. In his foreword to the report Prime Minister Gordon Brown says: "Food contributes over £80 billion to our economy and is our largest manufacturing sector, with food and farming employing 3.6m people".

Farmers are urged to produce more food more efficiently, while, unsurprisingly, at the same time being asked to reduce agriculture's impact on the environment and to cut their greenhouse gas emissions.

The strategy, however, is mainly aspirational, with only three pages of the 84-page report actually dedicated to the delivery of its aims. Partnership is the buzzword and there is certainly no mention of market intervention mechanisms to help farmers. The need for better research and development is acknowledged, but there is no talk of increased funding.

However, despite its shortcomings, Food 2030 has at least pushed agriculture up the political agenda and for that we should be grateful.

Food 2030 – the six targets

1. Enabling and encouraging people to eat a healthy, sustainable diet
2. Ensuring a resilient, profitable and competitive food system
3. Increasing food production sustainably
4. Reducing the food system's greenhouse gas emissions
5. Reducing, reusing and reprocessing waste
6. Increasing the impact of skills, knowledge, research and technology

PRIME COUNTRY PROPERTY MARKET BUILDS MOMENTUM

Prime country houses were unable to match the performance of farmland over the last decade and suffered badly during the credit crunch. However, a shortage of property for sale combined with renewed buyer confidence means prices started to recover during 2009.

On average, prices are still lower than they were 12 months ago, but there was strong growth across the UK during the final three months of the year, according to the Knight Frank Prime Country House Index.

Prime Country Property – price change by sector

Property Type	Quarter 4 price change %	Annual price change %	Average value £
Cottage	2.5	-1.7	0.45m
Farmhouse	2.6	-0.3	1.1m
Manor House	1.8	-5.7	2.6m
Unweighted average	2.3	-2.6	1.4m

Source: Knight Frank Residential Research

This resurgence was led by the London market, spilling out into the Home Counties and then trickling down through the rest of the UK. In the Home Counties, for example, average prices increased by over 5% in the second half of 2009, but rose by just 0.1% in the north of England and Scotland.

How the market performs in 2010 will very much depend on the volume of houses put up for sale during the year, but we expect prices to remain steady rather than fall or rise dramatically.

NEW PLANNING POLICY COULD PROVIDE BOOST FOR THE RURAL ECONOMY

A new planning policy quietly introduced by the government at the very end of 2009 could make it easier for farmers and landowners looking to set up new business opportunities in the countryside. Planning Policy Statement 4 (PPS4) – *Planning for Sustainable Economic Growth* – streamlines a number of other PPS documents and has been broadly welcomed by the CLA.

PPS4 looks at both urban and rural areas, but has dedicated sections on each. It still includes a number of vague statements such as "local planning authorities should ensure that the countryside is protected for the sake of its intrinsic character and beauty", but clearly recognises that rural areas do play a key role in the national economy.

It states that planning applications that "secure sustainable economic growth" should be treated favourably. This is defined as "growth that can be sustained as within environmental limits, but also enhances environmental and social welfare and avoids greater extremes in future economic cycles".

Local planners are also advised to accept that not all development in the countryside will be accessible by public transport, which has been a stumbling block for some projects in the past.

Full details of PPS4 are available on the website of the Department of Communities and Local Government.

PRIVATE WATER SUPPLIES UNDER SCRUTINY

Farmers and landowners with private water supplies could be affected by the new Private Water Supplies Regulations 2009 that came into effect on 1 January 2010.

The legislation applies to water used for human consumption that is distributed to more than one dwelling from either a private supply or is taken in the first instance from the mains and then further distributed via a private supply network. This will apply, for example, if the mains supply to a farmhouse is routed to secondary dwellings like holiday cottages. It could also apply if a farm or estate has farm buildings with kitchen facilities for workers.

Local authorities have until 30 June 2010 to provide a list of private water supplies and a risk assessment on each must be carried out within the next five years. Sampling will then be carried out to check on water quality with the frequency dependent on the results of the risk assessment.

Although the onus is on the local authority to carry out the assessment, it is worth bearing in mind, according to specialist law firm Burges Salmon, that the sanctions for breaching standards of water wholesomeness are serious and any breach of an enforcement notice served by a local authority is a criminal offence.

The property owner will also be liable for the cost of the risk assessment and sampling, although these will be capped at £500 and £100, respectively. **Knight Frank recommends a wholesale review of private water supplies on farms and estates. Please contact Edward Dixon or Alastair Paul for more details.**

CAP REVIEW STARTS NOW

The next reform of the Common Agricultural Policy is not due to be completed until 2013, but the tortuous process is set to start in earnest this year in parallel with discussions about the overall EU budget post 2013. Following the adoption of The Lisbon Treaty the European Parliament now has more influence over agricultural policy meaning negotiations will take even longer than before. The EU Commission is due to produce its first report at the end of this year and it is hoped the reform will be agreed by the end of 2012. However, with different blocs within the EU jockeying to ensure their views take pre-eminence it is unlikely to be a smooth journey. Reformist countries such as the UK and Sweden have reportedly been sidelined already by a group of 22 countries keen to safeguard direct support for farmers.

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READY TO HELP –

Knight Frank offers a wealth of in-depth specialised experience covering the rural property sector. Please get in touch with any of our experts if we can be of any help to you or your business.

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