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# Diversification and resilience of Welsh farming: prospects after Brexit

December 2019



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# Diversification and resilience of Welsh farming: prospects after Brexit

December 2019

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Any views are those of Professor Henley and Dr Morris and not those of Senedd Research.

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## Executive summary

The Welsh Government has presented proposals for future agricultural support after UK membership of the EU ends. These consultations provide for a transition to funding farmers as managers of a sustainable countryside environment for the benefit of wider society, beyond food production. Farm business resilience and the delivery of these wider 'public goods' will be a reflection of the strategic and operational stances taken by individual farming businesses.

However, farming businesses in Wales face a number of hurdles, such as poor upland land quality, and remoteness from centres of population. These factors severely restrict business resilience and revenue diversification strategies, such as improving farm efficiency, developing non-food and non-crop revenues, participation in agri-environmental schemes, or access to rural development funding and business support. When compared with England, Welsh farms are also smaller and less well resourced. This briefing provides an assessment of these issues, drawing on analysis of data from the annual England and Wales Farm Business Surveys, and provides an evaluation of business diversification as an option for Welsh farming policy post-Brexit.

The proportion of Welsh farmland which is classified as disadvantaged is very high, even in comparison to regions with similar landscape on the western side of Great Britain. Average farmer age is rising, and Wales lags in terms of the proportion of farmers that have further or higher educational qualifications. The proportion of farmers under the age of 45 in Wales has fallen from 14% to under 10% between 2010 and 2017. All these factors compound prospects for transition within the industry. One particular feature of current farming in Wales is the lower average levels of acquired funding from EU Pillar 2 agri-environmental schemes. In 2017 the average level of funding in Wales for farms applying for funding was £10,300, whereas in England the average was £13,600. Both countries have experienced a fall in take-up rates of Pillar 2 support, despite maximum permitted budget modulation in Wales.

Diversification activity on Welsh farms has grown over the past decade. However, diversification revenues on Welsh farms still represent on average only 3.4% of total farm revenues in 2017, compared to an average of 7.7% in England. In summary the proportion of total farm business revenue coming from non-food or non-crop



diversification activity remains low. This suggests that reliance on increased farm diversification to build resilience in Wales remains an optimistic strategy. In the worst case post-Brexit scenario diversification revenues might need to increase up to tenfold to replace other lost revenues.

In summary, farming household resilience relies, not only on food and diversified non-food income streams, but also on other income streams which are external to the business. A range of actions might support the continued growth in diversified income. While these might allow farms to contribute to providing wider social and environmental public goods, they may not support farming community identity and build economically sustainable farm businesses.

## Introduction

The potentially significant impacts of Brexit on the Welsh agricultural sector are an important consequence of the outcome of the 2016 referendum. The Welsh Government has presented proposals for future agricultural support after UK membership of the EU has ended via the two consultation documents '**Brexit and our Land**' (PDF, 3MB) and '**Sustainable Farming and our Land**' (PDF, 3MB).

These consultations provide for a transition whereby farmers are viewed as managers of a sustainable countryside environment for the benefit of wider society, beyond food production. The Welsh Government envisages that farmers will enjoy greater flexibility than under present support arrangements to choose strategies appropriate to their locational and business context, allowing farmers to both enhance productivity and to diversify into new business opportunities. This post-Brexit land management scheme sets out a medium and longer term vision. Longer term impacts will, of course, be dependent on resolving present uncertainties about future resourcing, which in turn hinge on UK Government budget decisions.

Should the UK Government not succeed in negotiating a new trade agreement with the EU after Brexit, the UK would default to trading with the EU on WTO terms. The immediate impacts of this on Welsh farming are likely to be felt through the potential loss of EU export markets for red meat in the face of imposition of high import tariffs. However, an assessment of medium and longer term impacts, on the assumption of subsequently negotiated free or low tariff trade arrangements, needs to be set in the broader context of an understanding of the resilience of Welsh farming.

**Resilience can be understood across various dimensions**, reflecting the range of strategic and operational stances taken by individual farming businesses. In the largely upland pastoral context of Welsh farming, these might include activity to improve farm efficiency, such as adopting precision breeding techniques and other activity to improve the effectiveness of animal husbandry. They might also include activity to take advantage of agri-environmental schemes, such as **Glastir**, and gain access to other streams of rural development (**EU Pillar 2**) funding and business support.

Given that the Welsh Government's proposals for future agricultural schemes are based on the provision of environmental 'public goods', farmers' role in environmental stewardship seems likely to continue. Access to post-Brexit business support for sustainable diversification activity will be conditional on completion of Farm Sustainability Review assessment. Followed by acceptance of a robust business case for proposed activity, demonstrating impact on the farm's sustainability across these economic, environmental and social dimensions. Diversification activity in the proposed approach, as set out in Sustainable Farming and our Land, focuses predominantly on rewarding farmers for providing non-market environmental and social public goods, such as carbon capture, protection of biodiversity, supporting public access to the countryside or protection of Welsh language and culture.

Finally and importantly, farmers face varied opportunities to develop diversified off- and on-farm, food- and non-food-related income streams. Farmers may have opportunities under the future approach to access business support, including advice, capital investment support and skills development, to promote other food and non-food marketable goods and services, conditional on a business case that these will enhance farm sustainability.

Future farming resilience in Wales will therefore rely on both demand-side opportunities to develop such activities. It will also rely on supply-side willingness and entrepreneurial ability to take advantage of opportunities as they present themselves to farming businesses. However, farming businesses in Wales face a number of hurdles, explored further in this paper.

One of the main hurdles is that, more so than in any other UK nation or region, poor upland land quality and remoteness from centres of population, severely restricts farming strategies. The extent to which farmers are able both to bring new farming technologies to bear on their agricultural output mix and intensity, and to take advantage of diversification opportunities is restricted.

In this paper we provide an assessment of these issues, drawing on analysis of data from the annual England and Wales Farm Business Surveys, and provide a summary of options for Welsh farming policy post-Brexit.

## Welsh farming in context

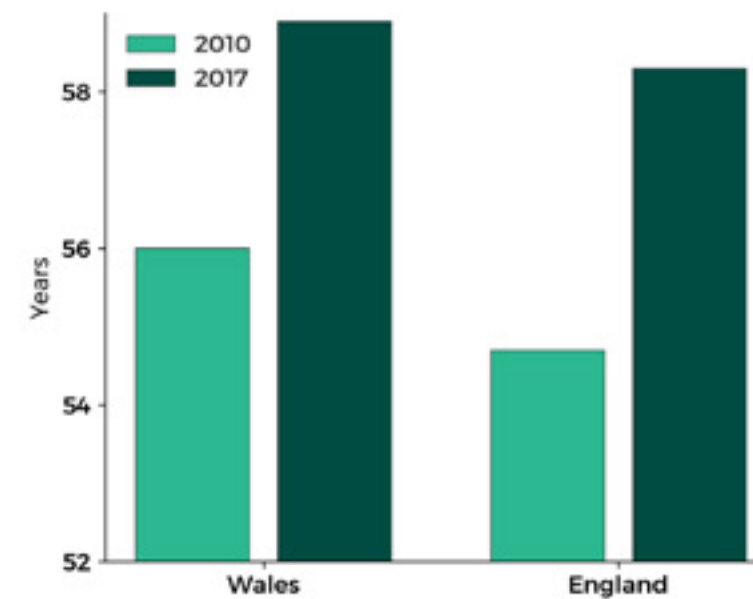
Welsh farms, as surveyed by the **Farm Business Survey** (which contains financial and physical data on 600 farms in Wales), have an average size of 120 ha of utilised agriculture area, which is around 70% of the average in **England**. Average size in Wales is smaller than in any of the English regions. 40% of surveyed Welsh farms are below 100 ha, compared to 25% in England. Within this smaller average size, there are very significant differences in land quality and, consequently, farming activity.

Over 75% of Welsh farmland is classified under EU designation of physical quality as less favoured, disadvantaged or severely disadvantaged, whereas in England less than 20% of farmland is similarly classified. Consequently, Welsh farming is predominantly pastoral (91% of all Welsh farmland). This is much more so than in any English region, even on the western side of Great Britain. The resultant effect being that farmland is not amenable to significant changes in farming patterns, even away from lamb production.

Research on farm diversification and rural entrepreneurship has highlighted the importance not only of farm characteristics, but also of the farmer and the wider farming family. It is well known that farmer average age has been steadily rising, and that younger generations of farming families are increasingly opting to leave the industry. However, the farmer age distribution is not dissimilar to age patterns observed amongst the **broader self-employed sector in rural areas**.(PDF, 970KB).

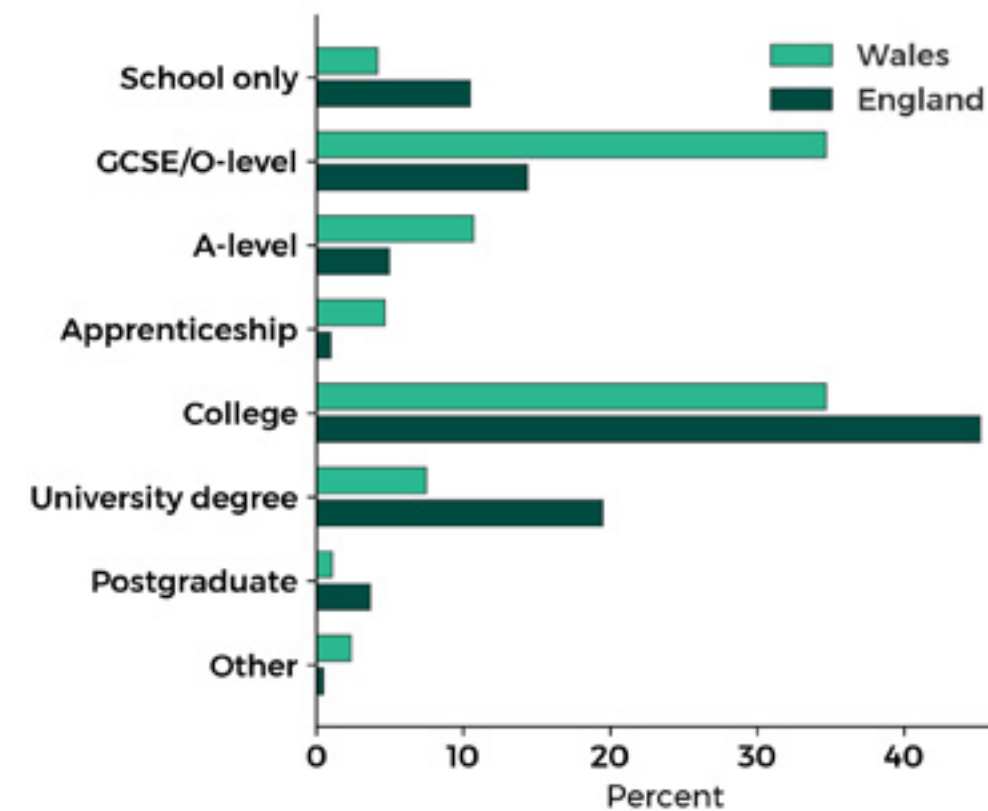
In Wales between 2010 and 2017, average farmer age rose from 56 to 59 years (see Figure 1). Similar averages and rates of increase are seen in all English regions. Increasing numbers of farmers have further or higher educational qualifications, although Wales lags behind England in this respect (see Figure 2). Younger farmers have higher average levels of education, and are more likely to have achieved industry-relevant qualifications at further or higher education level. So it is of concern that the proportion of farmers under the age of 45 in Wales has fallen from 14% to under 10% between 2010 and 2017 (although this ignores younger farming family members, with qualifications, who may succeed in due course into ownership on multi-generational farms).

Figure 1: Average farmer age



Source: Calculated by the authors using data from the Farm Business Survey

Figure 2: Farmer education levels, 2017



Source: Calculated by the authors using data from the Farm Business Survey

One particular feature of farming in Wales is the lower average levels of acquired funding from EU Pillar 2 agri-environmental schemes. This is despite the Welsh Government transferring 15% of the Common Agricultural Policy (CAP) Pillar 1 Basic Payment Scheme for 2014-2020 to Pillar 2 Rural Development Programme funding, the maximum permitted and the highest percentage across the UK. Take-up of these schemes reflects farmers' ability and willingness to identify non-food activity which might boost farm incomes. In addition **there has been criticism**, particularly from farming organisations, of the poor administration of these schemes. In 2017 the average level of funding in Wales for farms applying for funding was £10,300, whereas in England the average was £13,600. This appears to reflect differences in farm size and revenue capacity, since Pillar 2 funding in 2017 represented 4.1% of total farm turnover in Wales, but only 2.8% in England.

However, while across both England and Wales between 2010 and 2017 take-up rates of Pillar 2 support have fallen, in Wales they have fallen more sharply, from 87% to 55% of farms, and fallen from 6.0% to 4.1% of total farm turnover.

## Diversification patterns and trends

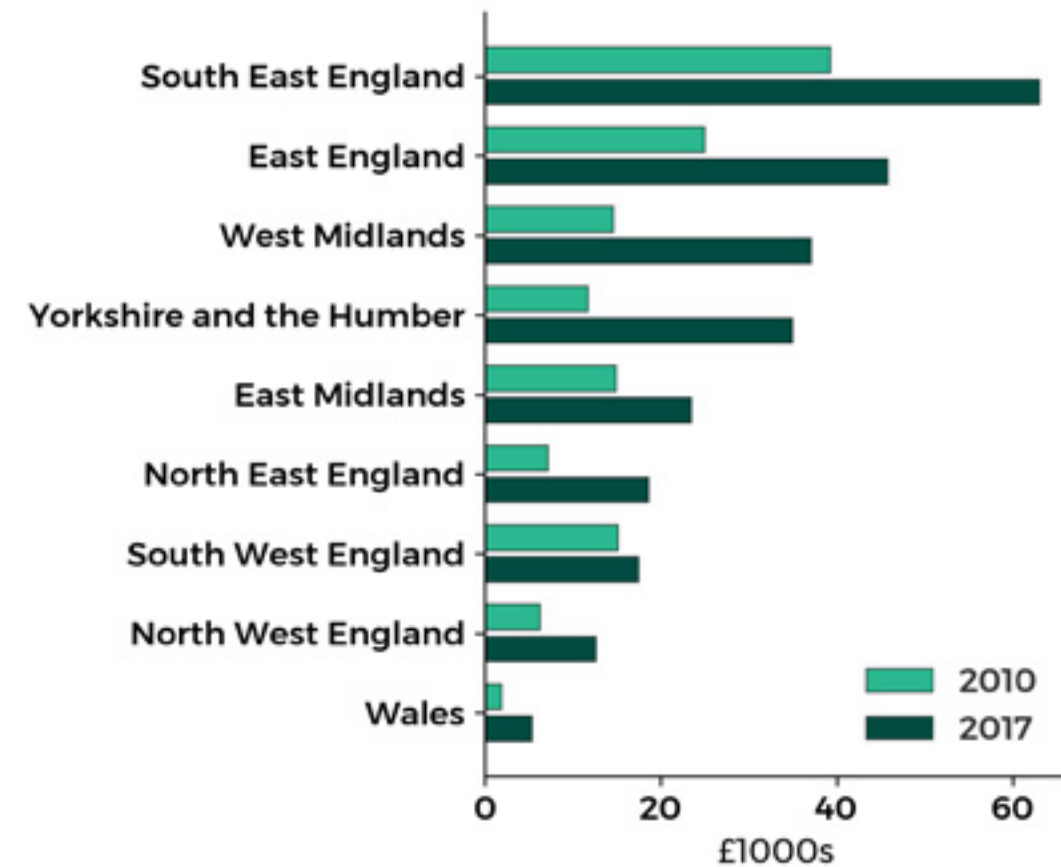
While agri-environmental scheme participation represents one potential revenue diversification for Welsh farmers, other forms of revenue diversification activity (detailed below) have seen significant growth and improvement. However, it is important to point out that revenue diversification on Welsh farms over the past decade has grown from a much lower base than in England. This low base again reflects the more challenging 'initial conditions' faced by Welsh farmers, in terms of land quality, farming mix, investment potential and access to markets.

The growth of non-crop (including non-livestock) diversified income streams has been a feature of recent trends in agriculture. Diversified farm activity falls across a range of activities: for example tourism-related and recreational activities such as operating holiday accommodation and caravan sites, children's farms, riding schools and livery stables, retailing activity of non-farm produce; and year-round non-agricultural property rental where farms have surplus housing or business premises, or have leased land for renewables generation or mobile phone masts.

Despite an almost tripling of diversified revenue between 2010 and 2017, average levels on Welsh farms are still much lower than in England (see Figure 3). Diversified revenues on Welsh farms still represent on average only 3.4% of total farm revenues in 2017, compared to an average of 7.7% in England. Profits from diversified activity in Wales are similarly lower; Welsh farms made an average profit from diversified

activity of £3,425 in 2017, much lower than in any English region. At the other extreme, average diversification profits in south east England were £32,073, where revenues in 2017 accounted for almost 15% of average farm business turnover.

Figure 3: Total farm diversification revenue by Wales and English regions



Source: Calculated by the authors using data from the Farm Business Survey

Revenues and profits vary considerably across different diversification activities, and the pattern observed across England and Wales reflects the strength of market opportunities and locational advantage. Over half of diversification revenues on Welsh farms are generated from non-agricultural purpose property rental. 30% of revenues are derived from a range of other activities not classified under the other headings, such as agricultural and non-agricultural hirework (See Figure 4). Revenue streams from tourism and recreational activities, although perhaps significant for a small number of farm businesses in Wales, account on average for a low proportion of total non-crop farm business revenues.

Figure 4: Diversification revenues by activity in Wales, 2017

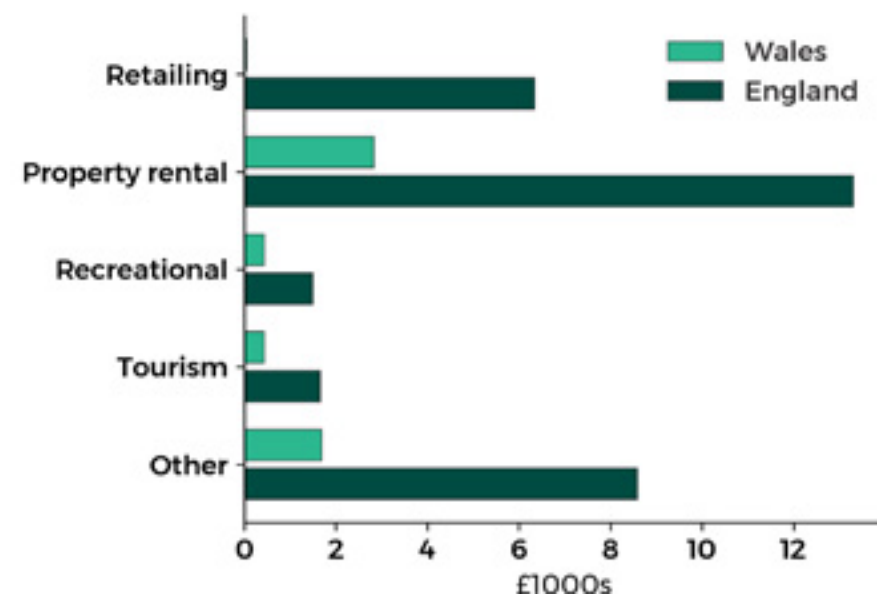


Source: Calculated by the authors using data from the Farm Business Survey

By comparison with England, average revenues for all diversified activity groups are much lower (see Figure 5). Even though in Wales rental receipts account for over half of diversification revenues, in cash terms the average amount is much lower than in England. This may reflect the much weaker residential and commercial property markets, and opportunities to achieve high rental levels.

Unsurprisingly it is farms in south east England that are able to achieve the highest levels of rental incomes, in 2017 generating over ten times the average amount in Wales. It is also of note that farms in Wales only generate tiny average revenues from retailing activity, in comparison to England. Retailing revenues are highest in the West Midlands and in south east England, suggesting the importance of proximity to major conurbations.

Figure 5: Diversification revenues by activity by country, 2017



Source: Calculated by the authors using data from the Farm Business Survey

In summary, despite promising levels of growth in diversification revenues and associated profits on Welsh farms, the proportion of total farm business revenue coming from non-food or non-crop diversification activity remains low. This suggests that reliance on farm diversification to build farm business resilience in Wales remains an optimistic strategy.

The data suggest that farm diversification in Wales is limited by absence of economic opportunity across various domains. Weak property markets and lower returns on property investments, lower market opportunities from remoteness from major centres of population, and lower levels of tourism revenue opportunities contribute to the issue. This is in comparison with coastal and upland areas in south west England, Cumbria and rural Yorkshire.

Further analysis of Farm Business Survey data reveals strong associations between diversification revenues, farm size and overall farm investment activity, particularly in buildings and in machinery. Except where farms have surplus residential accommodation, diversification requires investment. For example, caravan sites may require roadways and facilities blocks and retailing may require investment in manufacturing and packaging equipment.

Furthermore, in comparison to traditional upland animal husbandry or mechanised (and increasingly digitised) lowland arable farming, most non-property related diversification activities require significant labour inputs, and those inputs may be highly seasonal in nature, not necessarily fitting well with core farming activity.

Analysis also confirms previous studies, (such as **McElwee and Bosworth, 2010** (PDF, 4.52MB)) which show that diversification activity is also associated with farmer education levels, suggesting that such activity requires an ability to apply wider management skills, beyond those traditionally learned 'on the job'. All of these factors point towards the reduced extent to which relatively smaller and less well-resourced farms in Wales are able to use diversification strategies as a source of business resilience.



## Stakeholder stance and farming identity

Research studies highlight the traditional importance of food production to the sense of identity experienced by farmers and farming families (**Evans, 2009; Cheshire et al., 2013**). One consequence of this is that non-food diversification activities may be viewed by some farmers as ‘second-best’ in the face of pressure on farm incomes and where opportunities to improve farm efficiency are limited.

Particularly in Wales, farm businesses remain family businesses. On 55% of Welsh farms the spouse works on the farm – this proportion is higher than in any English region. Average levels of off-farm spousal earnings in Wales are low. Only 28% of farming spouses are employed off the farm, with a further 10% self-employed. Although these income streams clearly form an important element of household income, average annual spousal earnings in employment in 2016 were only £20,000, and from self-employment £13,000. For the significant numbers of farmers continuing to work beyond state pension age, state pension payments are also likely to comprise a significant element of household income.

Commentators and **industry bodies** also note that where diversification activity requires applications for funding from external sources, such as agri-environmental schemes, levels of bureaucracy and compliance monitoring serve as a discouragement. For example, **NFU Cymru has commented** that the proposed ‘advisor-led’ aspect of the proposed Welsh Government Farm Sustainability Review, which will unlock farmer access to future support payments, should not be seen as a remedy for overly complex scheme design.

Resistance towards non-food diversification strategies may be softened where there is a clear need and desire to ensure business succession to the next generation. Nearly half of Welsh farmers intend to hand the business on within the family, a proportion that is only slightly higher than that reported in English regions. There is some evidence in the Farm Business Survey that on farms where succession to the next generation is planned, diversification revenues are higher, and increased by a larger amount over the past decade. However, this may simply indicate the larger labour resource available within the farming family to support diversification activity.

The form of farm tenure may also influence diversification activity, as tenant farmers may encounter difficulties in securing landowner support for investments and changes of use. However, the proportion of farms which are owner-occupied or part-owner-occupied is higher in Wales than in any English region.

One further consideration is that highly diversified farms tend to be those which operate in limited company form, rather than as sole-traders or family partnerships. Large scale diversification may necessitate changes in the legal form of the business which many farmers and their families may be reluctant to consider.

To summarise, there are a number of factors, bound up in the structure and sense of identity of farming families, which may influence diversification activity and affect the extent to which farm business diversification is a feasible resilience-building strategy.

## Supporting policy options

The economic shock to Welsh farmers which would follow a Brexit which does not include tariff-free access to the EU Single Market is likely to be very large. **Tariff rates on sheep meat exported into the EU** vary according to meat type and level of processing, but range from 38% to 98%. In a scenario in which this market disappears completely, then average diversification revenues on Welsh sheep farms would need to rise tenfold from their current levels to offset the adverse shock to post-Brexit farm incomes.

Even allowing for some market substitution, and the potential offsetting benefits from sterling devaluation, as well as for targeted business support under a new funding settlement, there would still need to be very significant increases in diversification revenues. Given the physical, economic and social context set out here, this is likely to be a huge challenge for the industry to achieve.

Notwithstanding the unfavourable physical context, there is also a range of other ‘second order’ issues to consider which might facilitate farmers to achieve higher levels of diversification income. These concern education and training, entrepreneurial mindsets, and issues of farming identity. Appropriately designed policy intervention will need to address each of these, and will need to operate in partnership with agricultural colleges and farming organisations, as well as with other third sector and civil society actors.

Farm management capability is important and should not be ignored. Farmers who are expected to adopt an increasingly multifunctional approach to their business objectives are likely to experience significant future burdens on time and capacity, and this may limit their ability to respond to changing political and economic imperatives.



Diversification needs to be viewed as a collaborative endeavour rather than a competitive response, and to that end approaches based on establishing local learning networks may have merit. These might draw on the success of such approaches with other small business sectors, and form a significant element of education and training, to compliment traditional 'top-down' advisory and extension services support.

On the issue of farming identity, there is a particular concern that in 'pluriactive' farms, that is those where other family members leave the farm for much of the time to work elsewhere, the production of food risks being framed as a hobby activity. Consequently farm household resilience relies, not on food and diversified non-food income streams, but on other income streams which are external to the business. While this might allow farms to contribute to providing wider social and environmental public goods, it does not build economically sustainable farm businesses.

The issue of policy balance is critical. Ill-thought through policy configurations may lead to unanticipated second-order consequences, as farmers pursue objectives related to current short term funding programmes rather than longer term business sustainability. A balanced approach in the Welsh context might need to support the delivery of environmental public goods support, while not undermining the potential future development of the market for sheep and dairy products. These two need not be conflicting objectives. Similarly other diversification activity, which is not necessarily linked to delivering environmental public goods, might complement governmental policy priorities, by supporting wider local rural development strategies.

An emerging theme from farming organisations is the need to reduce the administrative burden which has been a feature of the current EU-funded agricultural support regime. However, there is a particular challenge here in balancing the legitimate concerns from farmers that replacement support schemes are easier to 'work', against the need for appropriate and robust levels of monitoring, evaluation and accountability. Good evaluation requires good provision of information. To this end policy makers and researchers would benefit from deeper knowledge of the wider economic and social circumstances of farming families, set in the context of the performance of the farm business. This requires information which reaches somewhat beyond the detailed on-farm revenue and costs data currently collected through HMRC returns and farming surveys.

