Market in Minutes
Q2 UK Farmland Market

July 2014

SUMMARY

The growth of best quality farmland continues to exceed expectations

■ Capital growth during the first half of the year has been strong for farmland, especially for the best quality and has exceeded our expectations. The average growth for prime arable land across Great Britain at 9.8% was almost four times that recorded for prime central London residential property at 2.5% for the same period.

■ The overall amount of farmland publicly marketed shows no sign of increasing above the historically low levels recorded since 2000; despite an increased number of small farms marketed since the weather improved.

■ However, the market remains diverse with quality and location being key to the strength of demand and consequently prices realised.

■ We have slightly upgraded our forecasts for 2014, but we do believe the first half of this year may have seen the lion's share of this year's growth. Weakening commodity prices and the threat of an earlier than expected interest rate rise are likely to impact on farm profits and cash flows as well as weakening market sentiment.

'The average growth for prime arable land across Great Britain was almost four times that recorded for prime Central London residential property'

Ian Bailey, Savills Research

Supply

The overall amount of farmland publicly marketed shows no sign of increasing above the historically low levels recorded since 2000.

Our research shows that the volume of farmland publicly marketed across Great Britain in the first six months of 2014 was 1% higher, at 82,350 acres, than in the same period of 2013 and very similar to the low levels seen over the last six years. The market started much later this year with two thirds of the land marketed in May and June.

In England, supply during the first half of 2014 increased just 3%, to around 59,500 acres, compared with the same period in 2013. However, there were significant regional variations (as illustrated in Graph 1). Activity increased considerably in the East of England (+87%) and the South West (+43%) although in both regions supply was particularly low last year.

The largest falls in supply were recorded in the North of England (-45%) and the South East (-17%). Slight decreases were seen in the counties across the middle of the country namely the East Midlands (-1%) and the West Midlands (-3%).

In Scotland, supply has been similar to the same period of 2013 (up just 1%) whereas in Wales supply fell by -24%. The supply data in this report is derived from publicly marketed farmland. Anecdotal evidence suggests the private market for farms and land remains active with some strong competition for good quality commercial units and rural estates.

Values

Capital growth during the first half of the year has been strong, especially at the top end of the market and has exceeded our expectations. Average capital growth of prime arable land across Great Britain at 9.8% was almost four times that recorded for prime central London residential property of 2.5%.

According to our Farmland Value Survey, growth during the first half of this year was concentrated in the second quarter along with the increased market activity. The average growth for prime arable farmland across Great Britain rose by 8.2% during the second quarter compared with 1.5% during the first three months of this year. The strongest growth was recorded in the West Midlands (18%) and the East of England (13.5%). Farmland values across Scotland remained unchanged and across Wales prime average arable values increased by 3.6%. However, average values hide regional variations which are illustrated in Graph 2.

The market remains diverse with value growth driven by local demand, quality and type of land and the residential aspect of the farm with the very best sales achieving well in excess of £12,000 per acre. The divergence of values continues with the best quality arable land recording the fastest rates of growth and poorer quality land the weakest. Compared with the figures quoted above for prime arable land, poor quality grassland value growth was recorded at 5.7%. Interestingly, growth for the poorest quality land has outperformed our expectations and may indicate that the upturn in the residential markets is already having a positive effect on the residential farms market which are often smaller livestock farms.

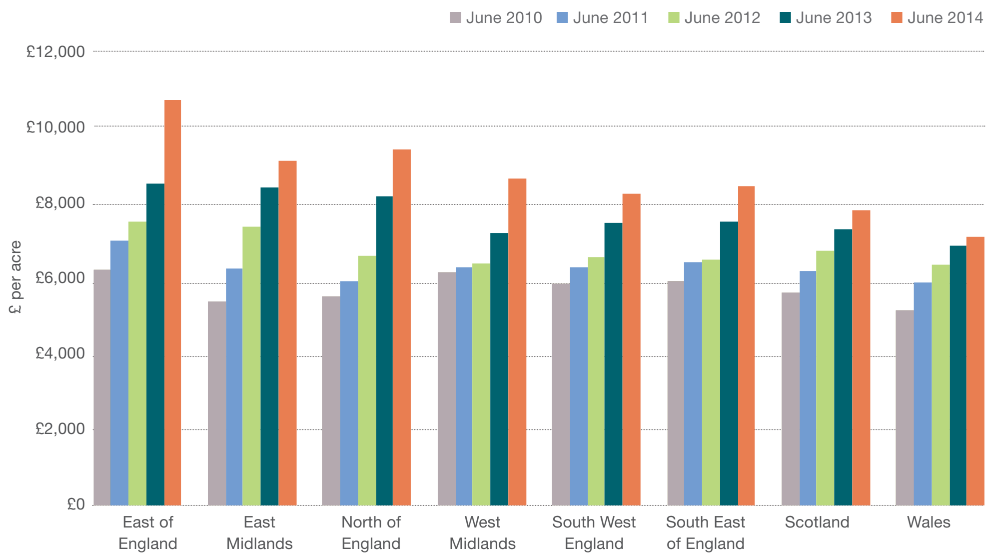
GRAPH 1

Regional farmland supply

Source: Savills Research

GRAPH 2

Regional prime arable values



Source: Savills Research

Buyers and Sellers

Our analysis of farm transactions, where Savills acted for the buyer or seller, for the first half of the year indicates that there was more selling activity by non-farming landowners than farmers.

In addition, our research indicates reduced selling activity from the corporate and institutional landowners. In fact, the figures suggest that net activity of these landowners appears to have shifted towards buying rather than selling.

So far this year, debt has not been an increased driver for selling farms. Debt related sales only increased from 20% in 2013 to 22% during the first half of this year. We expect this proportion to rise by the end of the year as commodity prices weaken and the prospect of an early increase in interest rates puts pressure on farm business profits and cash flows.

However, there appears to be an increase in 'retirement' related sales, these include those leaving farming and downsizing to a smaller unit. Our analysis shows these are all farmers, who are close to or have reached retirement age. This suggests they may be using the strength of the market to maximise the opportunities presented by the capital value of their assets.

Demand from non-farmer private landowners, whose primary motive was other than income generation from farming, has not waned. These, with farmer buyers, represent over 85% of all buyers creating the competitive demand driving capital growth.

Indeed, their motives tend not to be so influenced by the factors affecting farm profits and therefore will remain a key demand factor as commodity prices come under pressure. That said, farmers are still buying to expand their current farming business with expansion cited in 44% of all deals; representing the single highest reason for a farm purchase.

Cash, as the predominant source of buyers' funds, still features in 80% of deals, suggesting that demand for farms and estates is wealth driven. Therefore, increased interest rates will have more effect on supply than demand.

Farmland Index

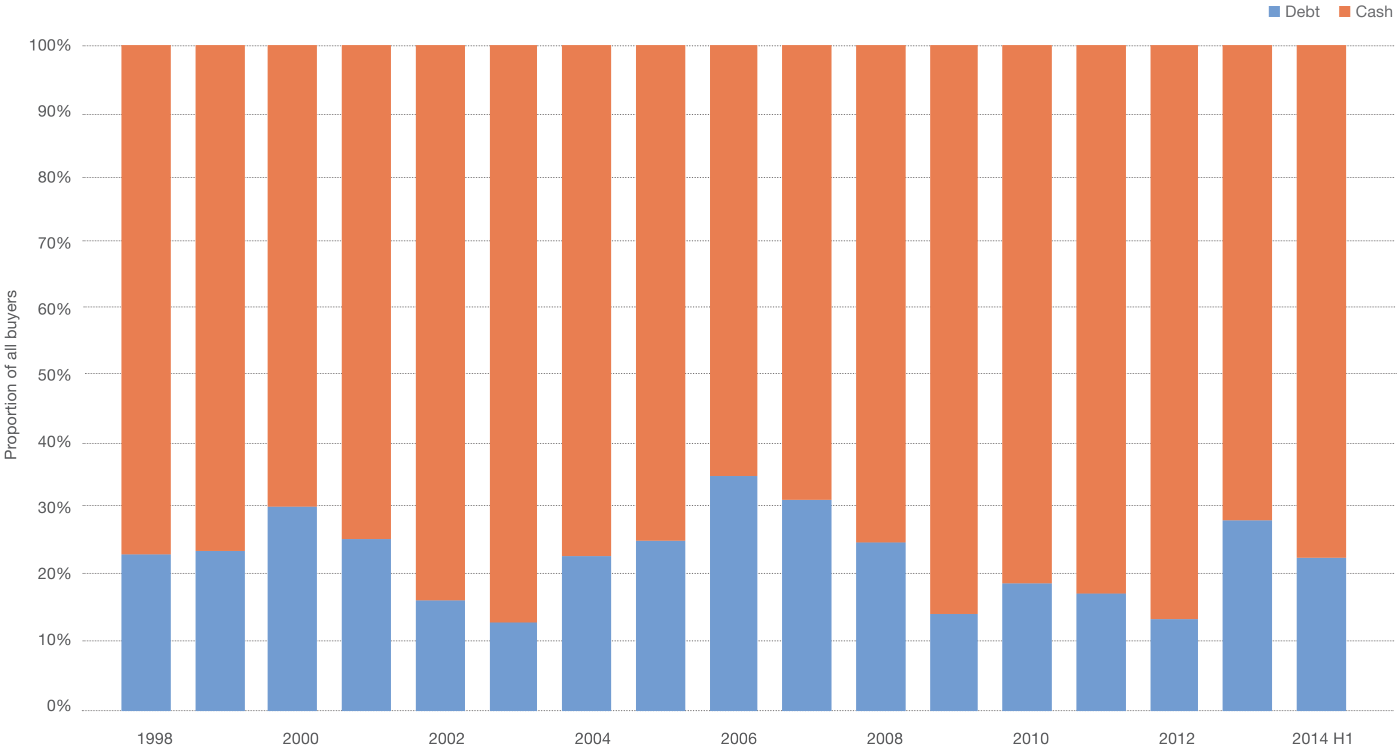
Interactive farmland value tool goes online

A new online graphic has been created by Savills. The British Farmland Price Index brings together a range of data spanning 1992 to 2014, the interactive value tool graphically illustrates the rise in the price of farmland – both arable and livestock – across eight different areas of Britain.

Just click on a region to see the data. It can be found at the following address:
www.savills.co.uk/farmland-value/index.html

GRAPH 3

Equity rich dominant demand for farmland



Source: Savills Research

Outlook

As we have noted, capital growth during the first half of the year has been strong, especially at the top end of the market. We have revised our forecasts for 2014, although we expect the increase in farmland values to be more muted during the second half of the year. However, our forecasts for 2015 to 2018 are unchanged and factor in the issues noted below.

Although the general economic outlook has improved, and this is forecast to continue, there are a few darker clouds beginning to shade farm profitability and cash flows.

These include:

- Commodity prices – the outlook is increasingly bearish across the arable and livestock sectors and not only for the remainder of 2014 but into 2015. On arable farms this may be alleviated by higher yields but as our Arable Benchmarking Survey for harvest 2013 shows, the average total cost of production for combinable crops was, at prices 20% higher than current prices, a significant proportion of crop price.

- CAP reforms, especially the new Greening measures, will have some impact on farm businesses and overall subsidy incomes will be reduced.

- Interest rates – an earlier than expected interest rate rise may add pressure to farm cash flows and investment plans.

- General election – the prospect of a change of government creates uncertainty although we don't expect this to have any real impact on the market.

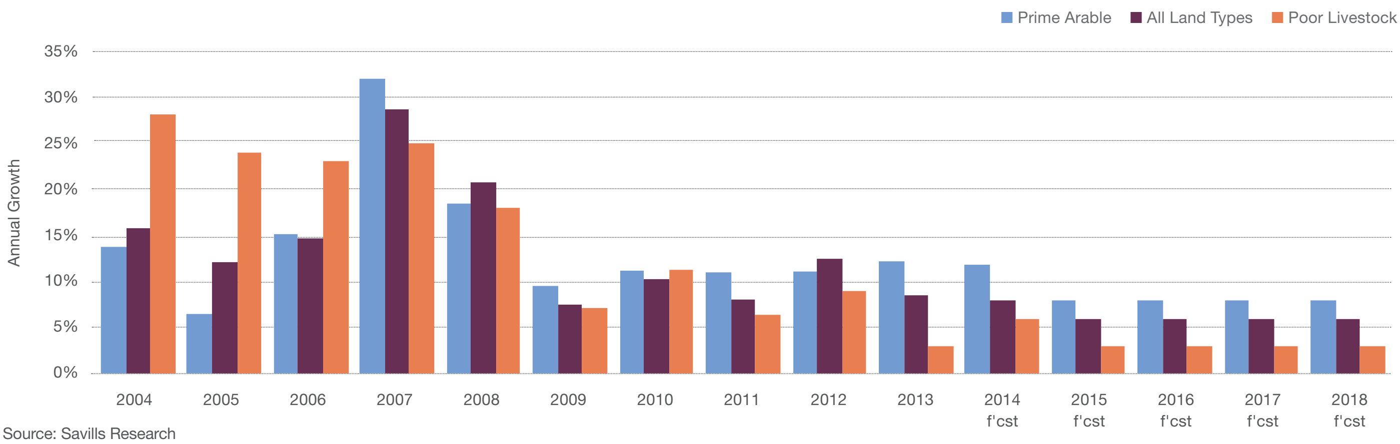
It is a tale of two parts:
On the one hand, we have the fundamentals of food production and food security competing with other land uses which include energy, new homes and infrastructure, and all against a backdrop of a finite and diminishing land supply in the UK. The uplift in the general economy will add more wealth and therefore potentially strengthen the demand from non-farmers to invest in farmland.

On the other hand, as often happens when the general economy picks up, prospects for farm incomes are dampened (farm incomes tend to be inversely correlated to GDP growth). Early interest rate rises, albeit from a very low base, may add additional pressure to cash flows on some farms.

We expect income pressure to bring additional supply to the market over the next 18 months, but it is unlikely to be significant enough to put downward pressure on values. The market will remain diverse with growth likely to be more muted across all sectors than has been recorded in the previous ten years and even more so than the past five years – see Graph 4.

GRAPH 4

Farmland value growth to soften over the next five years



Source: Savills Research

Savills Farm Agency team

Please contact us for further information

Ian Bailey
Head of Rural Research
01797 230 156
ibailey@savills.com

National
Alex Lawson
020 7409 8882
alawson@savills.com

South West
Penny Dart
01392 455 747
pdart@savills.com

Central/West
Richard Binning
01865 269 168
rbinning@savills.com

North
Andrew Pearce
01522 508933
apearce@savills.com

Midlands
Will Parry
0115 934 8034
wgparry@savills.com

East
Christopher Miles
01603 229 235
cmiles@savills.com

Scotland
Charles Dudgeon
0131 247 3702
cdudgeon@savills.com

South
David Cross
01722 426 813
dcross@savills.com

Wales
Daniel Rees
02920 368 915
drees@savills.com