

**CENTRE FOR  
RURAL RESEARCH**



**Farm Diversification in England 2002**

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**Centre for Rural Research, University of Exeter**

**&**

**Rural and Tourism Research Group,  
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## **FOREWORD AND ACKNOWLEDGEMENTS**

The primary aim of the study on which this report is based was to update a national study of farm diversification undertaken by the University of Exeter during 1989 to 1991. Although there really is nothing new in the practice of farmers using their farm's resources to produce non-food products, 'farm diversification' became a popular catchphrase during the 1980s as farm incomes came under serious pressure for the first time in the post-war period. With renewed policy interest in the concept, and considerable structural and other change in the agricultural sector in the intervening decade or so, it was time to look afresh at the role of diversification in farming.

The research was commissioned by the Statistics (Commodities & Food) Division of the Department for Environment, Food and Rural Affairs under the Department's rolling programme of policy evaluations and research. The work was undertaken jointly by the Centre for Rural Research at the University of Exeter and the Rural and Tourism Research Group at the University of Plymouth, during 2002. The research team comprised (for the University of Exeter) Professor Michael Winter and Martin Turner, who acted as co-directors of the study, with Donald Barr, who undertook the analysis of the data, and Mark Fogerty; and (for the University of Plymouth) Professor Andrew Errington, who led the Plymouth team, with Dr Matt Lobley, Matt Reed and Ian Whitehead, who were jointly responsible for the literature review. All have contributed in substantial ways to the research. The final report has been written by Michael Winter and Martin Turner, who also acted as principal editor of the report.

The research team wish to acknowledge the considerable help given by many people and organisations throughout the study. Sincere thanks are due to a number of staff in the Department for Environment, Food and Rural Affairs, particularly in the Statistics (Commodities and Food) and Farm and Animal Health Economics Divisions. The support and guidance of the Project Steering Group, comprising (for DEFRA) Stuart Platt, Michael Rowland, Dr Jane Hinton, Katrina Mullan and John Gorner, was appreciated by the team leaders, while Roger Price provided valuable guidance on issues associated with the income comparisons. The research could not have been undertaken at all without the cooperation of the many farmers who took time to complete the postal questionnaire, and those who further took part in the interview survey at a very busy time of the farming year. The staff of the Commissioned Work Programme Centres who undertook the interview study did so with their customary professionalism. The authors also gratefully acknowledge the part played by Marilyn Wills, who provided invaluable word-processing and administrative support throughout.

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## EXECUTIVE SUMMARY

### Introduction

#### *Research aims*

E1. This report is based on research undertaken to review the state of farm diversification in England analysing, in particular, developments during the past decade. The key aim is to identify the importance of diversified enterprises to farm business viability.

#### *Research objectives*

E2. The specific research objectives addressed by the research were as follows:

- **Objective 1.** To provide a review of the major studies of farm diversification in England carried out during the last decade since the previous national study.
- **Objective 2.** To examine how farm diversification has evolved over that period.
- **Objective 3.** To examine the nature and extent of the contribution of non-farming activities on agricultural holdings in England.
- **Objective 4.** To examine financial outlays and returns for diversified activities.
- **Objective 5.** To compare the relative economic performance of different activities.
- **Objective 6.** To examine what farm based resources are currently allocated to diversified activities, in particular with regard to labour and land.
- **Objective 7.** To examine the importance of diversified activities to the total incomes of farm households.
- **Objective 8.** To examine the extent to which the Rural Enterprise Scheme has stimulated increased interest in farm diversification since October 2000.
- **Objective 9.** To consider the outlook for developments in farm diversification.

### Background

#### *Policy issues in farm diversification*

E3. Diversification became a popular policy prescription in the 1980s as incomes from farming came under pressure due to over-production and consequent adjustments to the Common Agricultural Policy. This section of the report examines the development of relevant policies.

#### *The baseline study*

E4. The research seeks to up-date research undertaken by Exeter University for MAFF in the late 1980s. That research recorded 42.4 per cent of agricultural holdings in England to be involved in one or more of five defined enterprises (services, contracting, processing and sales, speciality products, miscellaneous).

E5. One of the most notable features of the diversified enterprises studied was the variation in their financial performance. The mean value of *output* was just over £22,000 per enterprise, but varied from a few hundred pounds to over £1 million.

Nearly two thirds of enterprises generated an output of less than £5,000. The average diversified enterprise earned a *net profit* of about £5,200 and an average *net margin* of just under £2,300 per enterprise. Thus, in most instances diversified activities were conducted on a relatively small scale and represented a minor income source, contributing approximately 11 per cent of total business income earned on the farms.

#### *Diversification during the 1990s*

E6. This section provides a review of the literature on farm diversification in the 1990s. During the 1990s a number of studies were conducted by academics and these are reviewed for what they tell us about the extent and nature of farm diversification. A key issue that emerges of particular relevance to this research, is the need for an operable definition of diversification for conducting empirical research.

E7. Farm households may have a variety of income sources, including employment off the farm (pluriactivity) and we gathered some information on this. However our focus is on the different possible combinations of capital and land assets. The definition used in the first baseline study is of *diversion* to other-income earning uses of any of the resources previously committed to conventional farming activities. This offers two difficulties: first, with regard to the definition of conventional agriculture as this will vary between times, places and people; and secondly with regard to the notion of the diversion of resources as this might imply that diversification only takes place if a farm household re-allocated resources within a particular time period.

E8. The report reviews a number of approaches to dealing with these problems. The diversified activities dealt with in this report were sub-divided into speciality crop or livestock products, on farm services, contracting services, food processing or direct marketing, and miscellaneous products or services. Each of these categories was sub-divided into a wide range of specific possible enterprises, making 92 in total.

## **Methodology**

### *Approach adopted*

E9. A postal survey was undertaken of a sample of English holdings, to establish the extent and nature of farm diversification nationally and to record the level of change since the baseline study. An interview survey was undertaken with a sub-sample from the postal survey to provide economic and social data on the operation of diversified enterprises.

### *The postal survey*

E10. The postal survey comprised a total of 5,500 questionnaires sent out, and produced a 'usable' response rate of 51 per cent, with no particular bias either by farm type or ESU size category. Geographically, the North East and North West Government Office regions produced below average rates of response at around 50 per cent while all the other regions were about average. Wholly tenanted holdings produced below average response with mainly owned above. Because the sampling (and response) rates were not uniform it was necessary to weight the data collected so as to reflect accurately the characteristics of the population of holdings.

*The interview survey*

E11. The sample was randomly drawn from the 1,716 postal survey respondents that had indicated some diversified activity.

**The nature of farm diversification**

*Patterns of diversification*

E12. Using the results of the postal survey, a total of 1,624 holdings (58.3 per cent) were found to be engaged in some form of diversified activity. Nearly one in five diversified holdings have no conventional agricultural production. Considered in the context of England's agricultural sector, therefore, it is estimated that about ten per cent of all 'farm' holdings are engaged only in diversified activities.

E13. It appears that larger farms are more likely to have the resources, flexibility and entrepreneurship to pursue diversification. Compared to the 'all holdings' average, diversification is significantly more common on 'cereals', 'general cropping' and 'mixed' farms, and notably less common on 'dairy' and 'cattle and sheep (LFA)' farms, and on 'other types'. These findings are consistent with the earlier study of farm diversification.

E14. Owner occupied holdings are less likely than average to be involved in any form of farm diversification, at 54.5 per cent compared with the 'all holdings' figure of 58.3 per cent. Wholly tenanted holdings are the most heavily involved, at 66.4 per cent. Sixty five per cent of full-time holdings are diversified, compared with 48 per cent of part-time holdings.

E15. There are notable variations in the incidence of farm diversification across regions, and between full-time and part-time farms within regions. A key finding is that at the 'all holdings' level, the North West has the lowest proportion of diversified farms (48 per cent) and the South East the highest (68 per cent). The same ranking is seen in respect of full-time holdings (the South East at 78 per cent, the North West at 53 per cent) and part-time holdings.

E16. More than two thirds of England's farmed area is closely associated with diversification. A further 4 per cent of land is held by farm businesses which do not themselves produce any conventional agricultural product, suggesting that approaching three quarters of the nation's farmland is associated with diversified activities. Key findings are:

- Agricultural services account for more than one in three of diversified farms (e.g. contract machinery services, machinery hire, consultancy and management advice and haulage provision of cold storage facilities and the supply of agricultural sundries).
- Trading enterprises are found on almost a third of diversified holdings. This group contains all those enterprises which involve the selling of agricultural or non-agricultural products to the general public.
- The provision of accommodation and catering services to the general public occur on 24 per cent of diversified holdings.



- Equine enterprises are found on nearly a quarter of diversified holdings.
- Nearly a quarter of diversified holdings recorded having at least one activity categorised as recreation and leisure services.
- More than one in five diversified holdings have an unconventional crop or crop-based processing activity.
- Sixteen per cent of diversified holdings are involved with unconventional livestock and livestock processing.

E17. The provision of agricultural services as a form of diversification is positively correlated with business size, with 58 per cent of 'very large' holdings involved. While most of the other enterprises do not show clear patterns in relation to business size, there is evidence that for a number of enterprise types, farms in the largest one or two categories appear to be more diversified than smaller units. This applies for 'accommodation and catering', 'recreation and leisure' and 'unconventional crops and crop-based processing'.

E18. The postal questionnaire addressed the issue of grant assistance for diversification. A little over five percent of all diversified holdings had received grant aid in setting up their diversified activities. This figure excludes the woodland grant schemes and also various agri-environmental schemes.

### **Financial aspects of farm diversification**

E19. This section draws on the interview survey of some 225 diversified farms in England, carried out during July and August 2002 in which we collected summary physical and financial data for diversified enterprises. This covered output, inputs specifically attributable to the enterprise and the estimated share of all other resources used by the enterprise. These included general overheads, labour (paid and unpaid family labour), machinery, buildings and rental charge (including an imputed 'rental value' on owned land and buildings).

E20. The report focuses on *net profit*, a measure of trading performance broadly consistent with that used in conventional accounting, and *net margin*, which is an estimate of the residual return to the entrepreneur's management skills and capital resources committed.

E21. The detailed financial results relate to a sample of 421 diversified enterprises on 225 holdings.

E22. The interview survey identified 445 diversified enterprises on 225 farms, of which detailed financial records are available for 421. Where the financial performance of these enterprises was adversely affected by the FMD epidemic, the estimated 'normal' position has been recorded so that the survey estimates provide an updated benchmark of farm diversification. The estimate of the contribution of diversification to aggregate agricultural income during 2001 is based on the actual position, and is thus fully comparable with the agricultural account.

*Enterprise output*

E23. The first indicator of scale in the diversified enterprises studied is *enterprise output*, which reflects the amount of resources committed and the potential for generating profits. The average value of output from commercial-scale diversified enterprises on farms in England currently stands at £25,500, with a range by type of enterprise of between £8,836 (equine enterprises) and £38,251 (agricultural services).

E24. The overall mean is clearly influenced by the scale of 'agricultural services', for which the average output is 1.5 times larger. This category is dominated by agricultural contracting, which ranges in scale from relatively small through to substantial business enterprises which in some cases dominate the original farm business. Two other types of enterprise recorded an average output significantly above the overall mean of £25,500, namely 'unconventional crops and crop-based processing' (£34,931) and 'trading enterprises' (£30,608). 'Equine enterprises' were by far the smallest in terms of turnover, at £8,836.

E25. Overall, more than four out of five diversified enterprises have an output below the mean, and this general characteristic is evident for all types of diversification. Thus relatively few large scale operations in each enterprise type tend to dominate the picture compared to the numerically much more important smaller scale enterprises.

E26. There is a general tendency for larger diversified enterprises to be located on larger agricultural holdings.

E27. Horticultural holdings have the smallest diversified enterprises, in output terms, closely followed by farms within the Less Favoured Areas. Both 'lowland cattle and sheep' and 'dairy' farms also recorded levels of output from diversification which were well below average. At the other end of the spectrum 'pigs and poultry' farms had a very large scale of diversification, with an average enterprise size some 2.7 times larger than the overall mean.

E28. Both of the Midlands regions, East and West, have the smallest diversified enterprises but record rather more enterprises per farm than average. The South West recorded the largest average scale of diversified enterprises, followed by the South East, and both regions recorded slightly above the overall mean in terms of the number of enterprises per farm.

*Enterprise operating costs and net profits*

E29. The sample mean value for retained profits from diversified activities – net profit as a percentage of enterprise output – is 27.8 per cent, giving an overall net profit of £9,474 per enterprise. With average operating costs of £16,026, direct costs represented about 43 per cent and overhead costs 57 per cent.

E30. Given the very obvious range in the sizes of diversified enterprises discussed above, a number of important features about farm diversification have been identified. This summary of the cost and profit structures of farm diversification highlights those which are important in understanding the nature of this form of farm business activity:

- On average, direct costs represent about 43 per cent of total operating costs, and overhead costs 57 per cent;
- However, cost structures vary widely by type of enterprise, with overhead costs accounting for between 36 and 78 per cent ('trading' and 'recreation and leisure' respectively) of total operating costs;
- The average diversified enterprise brings in a net profit per farm of £9,474, with a range by type of enterprise of between £5,617 ('trading enterprises') and £12,546 ('miscellaneous services');
- For all diversified enterprises, the average net profit margin is 27.8 per cent;
- Profit margins also vary widely by type of enterprise: they are lowest for 'trading enterprises' (at 18.4 per cent) and highest for 'equine enterprises' (at 64 per cent);
- Variability from the overall mean by enterprise type is greatest for total operating costs, particularly direct costs, and least for net profits, with variability in output levels somewhere in between.

E31. Based on these findings some broad categorisation of the various forms of diversified enterprise has been attempted. The one type of diversification which can be classed as high output, 'agricultural services', scores poorly in terms of *net profit ratio*, at least in terms of its relative ranking under this factor. Conversely, the two low output categories, 'equine enterprises' and 'accommodation and catering', also have the two highest net profit ratios.

E32. At the average levels of profitability identified by this study, it is very evident that farm diversification is making an important contribution to overall business profitability on many farms. Against the background of the farming recession, an average net profit of £9,474 from diversified enterprises appears to compare very favourably with the margins from conventional agriculture.

#### *Imputed costs and net margins*

E33. While net profit offers the best representation of enterprise performance in *financial* terms it is not a complete measure of the true costs, since it does not account for the value of the non-traded resources that are utilised in production. The costs associated with these resources have to be imputed, and relate to the unpaid labour of the farmer, spouse and family workers and the rental value of owned land. Deducting these additional imputed costs from net profit produces the *net margin*, the residual available to the entrepreneur as the two-fold return on (a) the investment in tenant's capital and (b) management performance.

E34. Because of the importance of land and family labour in the essentially family-based businesses of farming these imputed costs are typically significant elements in the overall cost structures of the industry. Thus, while the net profit may be high enough to suggest that the performance of the enterprise is satisfactory, the real *economic* outcome as reflected by net margin may well tell a different story. This is not to imply that the enterprise is not worthwhile, of course – the perspective here is principally that of the farming industry regarded as a sector of the national economy.

E35. The overall effect of accounting for imputed costs was to reduce the net profit by almost 40 per cent (£3,681), giving an overall net margin across all enterprises of £5,793. Although this varied by enterprise type, the differences were not as great as might have been expected: 'trading enterprises' and equine enterprises' fared worst, at £1,679 and £2,379 respectively; while 'miscellaneous services' achieved the best net margin at £9,311. The observed differences in cost structures mean that the rankings by type of enterprise change quite dramatically depending upon whether output, net profit or net margin is chosen.

E36. So what do these results mean show about the current profitability of farm diversification? Several important points emerge:

- The existence of healthy net profits (taken here to include both average profit *levels* as well as profit *margins*) in an era when profitability in conventional agriculture is weaker than for many years provides clear evidence of the importance of diversification as a feature of the modern farming sector;
- Furthermore, the not insubstantial average net margins obtained from diversification, irrespective of the type of enterprise involved, compare very favourably with mainstream agriculture at the present time;
- Clearly 'miscellaneous services', 'agricultural services' and 'accommodation and catering' are very attractive financially, returning substantial net margins on average;
- Those enterprises primarily connected with tourism and leisure (i.e. 'accommodation and catering', 'recreation and leisure' and 'equine enterprises') appear to be very useful adjuncts to a farm business, with the first two generating above average net margins and very good net profit margins also; equine enterprises are typically smaller, but as a group show the best net profit margin of all.

#### *The employment patterns of the farm family*

E37. A detailed examination of the structure, functions and degree of involvement and employment of the farm family was undertaken. These questions were addressed only on farms operated as family farms in the broadest sense. The work patterns of the individual family workers are often quite complex, involving different types of employment in different areas of the business or, indeed, in other businesses either on or off the farm.

#### *On-farm employment: agricultural and diversified enterprises*

E38. The pattern of employment on the farm was also examined, showing the labour input both on the farm and in the diversified business. These figures include non-family workers, the managers of corporate farms and also members of unrelated families farming in some form of partnership with the respondents. The key findings are:

- For this sample of farms, broadly similar numbers of people are employed in both the agricultural and diversified sectors of the business (627 in agriculture, 651 in diversification);
- The composition of the respective labour forces, however, is quite different: diversified businesses appear to involve relatively few full-time employment opportunities and a correspondingly high level of casual staff;

- This general finding applies to both family and non-family workers, although the overall level of non-family involvement is fairly similar as between agriculture and the diversified enterprises.

E39. One final area for investigation was the estimated proportion of the total hours worked accounted for by the diversified enterprises, with respect both to family labour and to the total available labour. The overall finding is that on these diversified farms the non-agricultural enterprises account for more than a third of the total family labour input and about the same proportion of the total labour.

#### *Length of involvement in diversification*

E40. The interview survey gathered information on the length of time each farm has been involved in farm diversification, based on the dates of establishment of current enterprises. On average, it was found that current enterprises have been established for 16 years, but the variation by farm business size showed a much lower average age for diversified enterprises on 'very small' farms, at 11 years. The data appear to suggest that the pace of diversification has steadily increased over the period, from 1.5 enterprises per farm in the early years to 2 in 2002.

#### *The aggregate income from farm diversification in England*

E41. Two levels of comparison between the incomes generated respectively by farming and by farm diversification have been made: at the farm business level for diversified farms, and at the England level. It is clear that diversification makes a major contribution to 'total business income' on many diversified farms, with its average share of the total (before allowing for the value of the labour of the farmer and spouse) ranging from 24 per cent on dairy farms to 103 per cent on lowland cattle and sheep farms.

E42. Although direct comparison with the aggregate income from agriculture in 2001 is not possible, it is concluded that farm diversification produced a total of some £785 million in that year. It is further estimated on the basis of the 2000 data that, assuming a similar level of income from diversification, farming activities alone would have produced an aggregate income of £1.03 billion. It is concluded that, in broad terms, farm diversification contributes about 43 per cent of the total aggregate income from agricultural holdings of £1.815 billion.

### **Dynamic aspects of farm diversification**

#### *Comparison with the original baseline study*

E43. One of the principal objectives of the present study has been to update the 1989/91 study to provide a new baseline from which one aspect of the structural adjustment of the agricultural sector over the next few years - the diversion of resources from food production towards alternative uses – can be judged.

E44. In the previous study it was noted that, notwithstanding the results from the financial accounting undertaken in the survey, four out of five diversified farmers considered their diversified enterprises to be successful in the context of their own

particular objectives, and almost one third had intentions to expand or to introduce new ventures. This discussion focusses on the directly comparable findings of the two studies to set the scene for a review of the dynamic aspects of farm diversification.

E45. For a number of reasons direct comparisons with the 1989 postal survey are far from straightforward. **Because of these differences in methodology there are small variances between data presented in this section and certain corresponding figures found elsewhere in this report.**

#### Survey response

E46. The usable response achieved in the 2002 survey is markedly lower than that of its predecessor, at 49.6 per cent compared to 69.2 per cent (England only). Probably the most important factor influencing the lower response rate was the timing of the postal survey mail-out, which coincided (late April) with a particularly busy time of year for livestock and crop farmers alike. It thought likely that a number of other factors were also involved since, within the overall response, the pattern found is broadly similar.

#### Defining farm diversification

E47. The earlier discussion touched on the range of uses of the term 'diversification' and identified the conceptual approach used in both the present and the previous surveys. However, although both surveys use a common basis there are necessarily certain differences of definition between the main analyses used for the 2002 survey and the 1989 report. In this section, therefore, the definition of diversification used for these comparisons has been adjusted to be the same as that used in the 1989 survey. **It should be noted that this definition differs from that used in the main body of this report both by the inclusion of organic production as a diversified activity in itself and the exclusion of the leased farm resources.**

#### The incidence and structure of diversification

E48. The data would appear to confirm anecdotal evidence suggesting a substantial increase in the proportion of holdings engaging in some sort of diversified activity between 1989 and 2002. At regional level farms in the North continue to be the least likely to be diversified and those in the East the most. Diversification in the West region has shifted from being below the England average to being slightly above.

E49. The incidence of the five broad 'enterprises' indicates some changes in the relative importance of the *types* of diversification. The proportion of all farms engaged in each of the enterprises has risen, but only marginally in the case of contracting. This 'deepening' of diversification is confirmed by the marked increase in the proportion of diversified holdings engaged in two or more enterprises rising from 29.6 per cent to 52.1 per cent.

E50. The first thing to note about the levels of diversification of the different groupings is that the proportion of holdings that are diversified has risen right across the board, without exception. This finding not only adds depth to the headline increase in the overall incidence of farm diversification but also clearly suggests that farm diversification is now a major development shaping farming with widespread implications for the rural economies of England, and important policy ramifications.

E51. The degree of increase in diversification, however, has not been evenly distributed, so that now there is clear pattern related to farm business size. Larger farms are more like to be diversified, and this tendency is much more pronounced now that it was in 1989.

#### Length of time in operation

E52. There is a significant reduction in the proportion of recent 'enterprises' that is, those less than five years old, compared with the 1989 findings. One important conclusion from this is that the policy impetus given to farm diversification in the second half of the 1980s did 'kick-start' a significant increase in the numbers of farmers engaged in some form of diversification, and that this pattern was reflected in the 1989 findings.

#### Prospective developments

E53. Perhaps surprisingly, respondents' future expectations with regard to diversification seem to have been broadly similar in 2002 to those recorded in 1989. Even though the current level of diversification is considerably higher than it had been at the time of the earlier survey a similar number of respondents indicated that they were 'definitely' going to introduce a new activity. The activities cited were concentrated in both years in the 'services' and 'miscellaneous' categories. In 2002 slightly fewer already diversified holdings than previously were planning to expand an existing activity, but in both years only a very small proportion were planning to give one up.

#### Baseline studies of diversification: a summary

E54. Despite the methodological difficulties in comparing detailed results from the 1989 and 2002 studies of farm diversification, the findings in this section have identified some fascinating developments in the incidence and patterns of this form of business growth. Some of these have very obvious implications for rural policy, while others confirm both the pace and, in this area at least, the direction of change if the nation's farming sector.

E55. During the intervening period between the two studies farming has experienced 'the best of times' (the unpredicted boom in farm incomes between 1992 and 1997 following sterling's ejection from the Exchange Rate Mechanism) and 'the worst of times' (the multi-faceted farming recession since about 1998). Whatever the pattern of establishment of new diversification enterprises during the 1990s, careful comparison between the updated baseline study and its 1989 predecessor has identified:

- Diversification has increased substantially both in terms of the proportion of holdings reporting some diversified activity and in terms of the number of diversified 'enterprises' that the diversified holdings are engaged in;
- The one area of diversification that has seen relatively little growth is machinery contracting;
- The widening of diversification has encompassed all groups of holdings: LFA and non-LFA, all farm types and all farm sizes;
- The greatest increase in the proportion of holdings with some diversified activity has been in the larger holdings;

- The number of enterprises established for more than five years has shown a significant increase;
- The proportion of respondents planning to introduce new activities has remained about the same, while those planning to expand existing activities has fallen.

*Drivers of business and income diversification*

E56. A very wide range of factors are involved in the evolutionary development of a more diverse, less agriculturally focussed, farming sector in England. The present study identifies the income factor (that is, the financial need to find an alternative, supplementary source of income) as quite clearly the most important motivation behind the establishment of a diversified enterprise, with six out of ten listing 'increase family income' and more than four out of ten citing 'maintain family income' principal causal factors.

E57. However, a wide range of forces are involved in the diversifying of English agriculture, many of which are associated with the opportunity afforded by the development of a new, non-agricultural enterprise to make better use of existing farm resources. Other important motivations lend further emphasis to the attitude of mind which many identify as a central element in successful diversification. More than a fifth considered that the diversification would enhance the asset value of their farm, an interesting observation which suggests that at least some diversifiers may have an eye on their ultimate retirement or, at least, the sale of their present holding.

E58. An element of serendipity is introduced by the finding that 17 per cent of diversified respondents had grown their enterprise from what was originally an informal hobby while, in keeping with the small scale of many such enterprises, 16 per cent still regarded their diversification as little more than indulging an interest or hobby. Overall five per cent had established a new, diversified enterprise in order to create employment for family members. As would be expected, these general findings vary very substantially according to the type of enterprise involved.

*Establishment of diversified activities*

E59. The postal survey explored the nature of recent changes affecting one or more of a respondent's diversified activities, providing a number of alternatives to obtain a broad indication of change in the diversified sector. The results give an interesting overview of recent change in farm diversification, suggesting that 16 per cent of all holdings started, and a similar proportion expanded, a diversified enterprise during the past five years. For already diversified holdings, however, the equivalent proportions are about 27 per cent.

E60. The data show that the largest concentration of new activity has been in 'miscellaneous services' (at 23 per cent of all new business activities), followed by 'trading' and 'accommodation and catering' activities (both at 16 per cent). Relative to the total number of activities in each category, however, a slightly different picture emerges. Although total new provision is slightly more evenly distributed than the foregoing analysis, the largest expansion has been in the 'accommodation and catering' group, closely followed by the 'equine' and 'miscellaneous services' groups.



E61. One of the conclusions from this analysis is that farmers are less likely to initiate new business activities in types of diversification of which they have no experience than they are for those in which they are already active. It should be noted that, in this study, a distinction is drawn between *activities* and *enterprises*, the latter being regarded as broadly equivalent to an integrated business unit. On this basis, it may be stated that (a) more than a quarter of diversified holdings have established at least one diversified *activity*, and (b) nearly one in five have set up a diversified *enterprises* in the last five years. These are key findings which highlight the continuing dynamics of farm diversification in England.

E62. Earlier it was seen by comparison between this study and its 1989 forerunner that some 15 per cent of all holdings may have become diversified over the thirteen years between the two studies. Consequently, the finding that only an additional three per cent of holdings have diversified for the first time over the past five years could be taken to suggest that there has been a significant slowing in the pace of change, but some care is necessary in interpreting this information.

E63. Perhaps the most striking finding from this analysis is the remarkably widespread pattern of continuing diversification, with substantial proportions of each of the sub-groups examined recording recent diversified activity. These data provide an unequivocal indication of the strength of this movement towards more diverse farm businesses, and may also be read as evidence of a broad-based and fundamental shift in the outlooks and expectations of the farming community.

E64. Even so, there are distinctive regional differences in the pattern of new diversification, among the most notable of which is that more than a third of recent diversification has occurred in the South West. The next most active region for the establishment of new diversifications was the South East. Although less diversified as a group, 'small' and 'very small' holdings have nevertheless seen significant developments in diversification over recent years.

E65. It was found that 'miscellaneous services' activities represent the category of diversification most likely to have been improved over the last five years, followed by 'accommodation and catering'. The latter finding probably reflects, at least to some extent, the market requirement for improved quality in such ventures. Again, though, it is clear that there is an across-the-board pattern in the *expansion and improvement* of diversified activities, much as was seen in terms of newly established ventures.

E66. The study looked at changes to diversified enterprises over time, and found that a third or more of recently established activities were subsequently expanded or improved, reinforcing the picture of a vibrant, expanding business sector. While it is likely that many of these expansions and improvements form part of an original business plan, this finding does suggest that a significant proportion of new diversified activities perform well enough in the early years to encourage further investment.

E67. In terms of problems with diversification, the notable finding is that more than six out of ten diversified enterprises were apparently set up without any real degree of difficulty – certainly nothing that, in retrospect, stood out as a major problem at the time the operator completed the questionnaire. Even so, it is clear that many who are

new to diversification can expect to encounter a wide range of problems ranging from such fundamentals as the nature and strength of market demand for the product or service, through aspects of the business background and personal skills of the entrepreneur to various regulatory issues.

*Success and failure in diversification*

E68. The issue of the respective success and failure rates of new diversified enterprises has important implications for agricultural and rural policy. One of the broad conclusions from this study is that on about one in three of diversified enterprises the owner has been sufficiently confident of its business potential to invest further in either expansion or improvement subsequent to its establishment.

E69. The interview survey provided an opportunity for the in-depth investigation of the pattern of development of diversified enterprises over time, and it was found that there is a degree of solid continuity, with nearly half (47 per cent) which had not changed the current enterprises since establishment; and 44 per cent do not envisage changing their enterprises over the next five years. Interestingly, the dynamics of both 'very small' and the 'very large' farms appear to be different from others, in that they are seen to be more likely both to have given up a diversified enterprise and to be considering a new one.

E70. The study also looked at failed diversification, and found that the overall percentage of holdings having given up at least one diversified activity in the five years prior to the survey was about four per cent. It should be noted that this figure refers only to those cases where the farm itself has remained in business: what cannot be known from a survey of this type is either the number and type of diversified activities that have closed together with the parent farm business on which they were situated, or the connection between (nor the nature of causality) these two events.

*Successful diversification: a review of the survey evidence*

E71. The survey evidence of the reasons for success in farm diversification shows that, as would be expected, most respondents cited a number of reasons for the expansion of their diversification but, in contrast to the findings with regard to closures, a business focus is very evident in expansion. Thus, 63 per cent mentioned 'market conditions', 54 per cent the need to 'improve or maintain margins', 32 per cent the need to 'improve or maintain competitiveness'. More apparently opportunistic reasons also feature, such as 'availability of buildings' (22 per cent), 'availability of machinery' (17 per cent) and 'availability of labour' (17 per cent).

E72. These and some of the other reasons cited for expansion begin to identify and define a group of people with a developed (or developing) entrepreneurial approach to business growth, seeing opportunities for re-deploying resources of land (including buildings) labour and capital to more productive and profitable uses. In stark contrast to the grant-aided expansion of much post-war agricultural activity, this is clearly not an option in modern diversification and yet the sector is apparently thriving.

E73. A similar picture of a strongly market-led approach in the development of diversification emerges from the analysis of the reasons for upgrading diversified activities. Major factors influencing the decision to upgrade the activity in some way

include 'response to customer demand' (62 per cent), to 'improve or maintain competitiveness' (55 per cent), to 'improve profit margins' (37 per cent) and to 'establish a niche market' (26 per cent). This further strengthens the perception that the drivers of successful farm diversification are much more likely to be 'market-led' than 'input-driven'.

E74. This analysis is taken further, with respondents' own perceptions of the reasons for the profitability of their enterprises identifying a broad range of 'success factors' in successful and profitable diversification, among the most important of which are:

- 'Good market for product' (all types);
- 'Family involvement and commitment' (most types not independent on family);
- 'Good proximity to market' (depending on type);
- 'Attractiveness of location' (for accommodation and leisure activities);

E75. While a number of other factor such as 'management ability', 'level of capital investment', 'good marketing', 'competitive advantage' and 'market research' are clearly very important, respondents' assessments of the principal factors underpinning their profitability may be summarized as *market-led*, *personal commitment* and *location*.

E76. Perhaps of equal importance in assessing success is a clear understanding of the reasons for a current lack of profitability. In fact, of the seven per cent who knew their enterprises were unprofitable, nearly half (45 per cent) expected this to be a short-term problem because the enterprise was in the start-up phase when losses were to be expected. However, nearly a quarter reckoned that the market for their product was not strong enough, while 19 per cent identified a 'lack of competitive advantage' as a major factor. Nine per cent blamed 'inadequate marketing' for the problem of a lack of profitability.

E77. A final perspective on successful farm diversification is respondents' assessments of the factors (including profitability) which they regard as being important indicators of success. While two financial measures - 'cash flow' (66 per cent) and 'profitability' (61 per cent) - come top of their list, it is clear that these farmers take a very rounded view of 'success' in assessing their diversification. Synergy with the remainder of the business is very important (56 per cent), but so is 'customer satisfaction' (53 per cent). Personal and family satisfaction is also widely seen as important, including 'fitting in with farm life' (41 per cent). 'operator satisfaction' (35 per cent) and 'family employment' (21 per cent).

E78. This study has both confirmed and strengthened many of the findings of earlier studies about the dynamic nature of farm diversification as a largely market-led adjustment in farm resource use, a process which is a growing part of the farm sector's adaptation to the new economic and policy environment in which it increasingly operates. However, the diversion of 'agricultural' resources into diversified enterprises can take place only as fast as the markets for those particular products and services grow. Far from being recent discoveries, many of these markets have been growing steadily over many years. As they have grown, so

enterprising farmers have seen the potential for business activity, established new 'diversified' enterprises and catered for the consumer demands they expressed.

E79. Along the way, there has been a major change in attitudes among many owners of agricultural resources. There is a now among farmers a growing recognition not only that agricultural resources can validly be used for forms of economic activity other than food production, but also that this wider definition of their role makes sense in meeting the wider needs of society in the twenty first century. It is against this background that the prospects for the future development of farm diversification are now discussed.

*Prospective developments*

E80. The study concluded with a careful review of respondents' plans for new diversification ventures over the next few years. It was found that nearly half (46 per cent) of currently diversified farmers plan to introduce a new diversified activity in the foreseeable future, either in conjunction with expanding an existing activity or as a stand-alone venture. More than half (56 per cent) plan to expand an existing activity, many of which will be in conjunction with setting up something new. Only 1.5 per cent plan to give up an existing diversification.

E81. The *types* of diversification in which these already diversified farmers see most potential make interesting study, with most seeing potential in various parts of the service sector. Some 42 per cent of the planned new activities will be in the area classified as 'miscellaneous services', and 27 per cent will be 'accommodation and catering' activities. No other category of diversification comes close in terms of planned development to these two types

## CONCLUSIONS AND RECOMMENDATIONS

Rather than select and repeat the key findings of this report, which are already set out in the executive summary and in the body of the report itself, this short concluding chapter reflects and comments on a few key themes of the research. It does so particularly in the context of changes since the earlier Exeter research. In addition, it makes some recommendations on how we feel research in this area should be carried forward.

In examining our own findings against those of the original baseline research (McInerney and Turner, 1989), as undertaken in some detail in Chapter 6, we are struck in general terms by the similarities between the findings of the earlier study and are own. Indeed many paragraphs from the conclusions of that study could be placed verbatim into our conclusions without doing any real disservice to our own findings. For example,

It has to be said, too, that although diversified enterprises are common in farming many of them are relatively unremarkable, and some almost qualify for being considered as traditional activities. Machinery contracting and provision for farm-based tourism, for example, have long been accepted sidelines to farming. It is the more eye-catching but infrequent examples - like snail farming, golf courses, crops of evening primrose and craft workshops - that dominate media attention and create a rather biased image of the change that is taking place in the countryside. It is certainly true that there are many ways in which rural resources can be used productively for things other than conventional food production. The demand for these uses (whether in the form of consumer products or services) appears to have grown over recent years, and those demands are likely to expand and widen in the future as food production loses its exclusivity as the primary use for agricultural land. It is also true that, as the incomes from farming have seemed less secure many operators of agricultural holdings have been looking to see whether any of those alternatives were relevant to their businesses. As a result there has been a noticeable expansion in farm diversification in Britain in the last decade. But it is important to emphasise that this is less the discovery of new openings than the manifestation of a predictable development in the rural economy. In many ways the widening of business activity on farms is no more remarkable than the diversification of petrol filling stations into the sale of food products, magazines, digital watches and other commodities that might serve the needs of passing motorists. It is simply the kind of exploitation of valid market opportunities that every resource owner or manager is expected to do in every sector of an enterprise-based economy ... (McInerney and Turner 1989)

These words could have been penned with equal validity for the present study. The activities characterised as diversification remain unremarkable both in terms of their characteristics and in terms of an economic understanding of market responsiveness. Of course the scale and extent of diversified activity has continued to grow, thereby reinforcing the thrust of the earlier remarks and the implied prediction that things would continue as they were in the 1980s. Thus our study shows a continuing process of agricultural adjustment and the growing significance of diversified activities within

the rural economy, an economy which is itself more complex and diversified thereby providing many of the opportunities for farmers to diversify.

The criteria for success in diversification remain broadly the same as in the 1980s. These include the existence of a market opportunity, the necessary on-farm resources (such as specific expertise, management skills, marketing ability), and the need for careful scrutiny and assessment of business potential. Again, as in the earlier study, we did not discover successful farm diversification to be particularly relevant to small or to struggling businesses. On the contrary, it is hardly surprising that most successful diversified enterprises form part of an otherwise successful farm business and, quite often, these are large businesses with, on occasions, diversification having served to facilitate expansion of the enterprise as a whole.

However, this last point brings us to some comments on where things may have changed since the earlier study. Clearly the continued expansion of diversification, both in terms of the number of farmers operating such businesses and the scale of diversified enterprises, brings into question the maxim from the early years of growth in diversification (the 1970s and 1980s) that such enterprises should be supplementary to the farm business. This was the line taken by leading farming commentators and spokespersons when diversification first hit the headlines. The message to farmers was a simple one, albeit somewhat caricatured here: 'diversify if you wish but don't forget that farming is your core business.' By implication, this message implied that farming itself was of inherent importance and its role in the national and rural economy should be affirmed and protected.

The context in the twenty first century is rather different. The current policy framework, including the recently published *Government Strategy for Sustainable Farming and Food*, places considerable emphasis on diversification as an element in rural and agricultural recovery. Moreover, we found many more cases than in the 1980s where the diversified enterprise assumed a greater economic significance than the farm itself. In the light of CAP reform proposals to de-couple support payments from production, it is logical to assume that the extent of these cases will increase. Farm diversification is no longer merely a modest supplementary adjunct to the core farm business.

This brings with it another set of social differences between the current situation and that of the late 1980s. There are two key issues here. The first is that, in the context of both the increased level of diversified activity and the parlous state of farm incomes (far worse than in the late 1980s), some farmers ill-suited through lack of capital or expertise to diversify may be encouraged to diversify, with predictable and lamentable consequences for their own business circumstances. Whilst we found relatively few examples of this, we did observe that diversification as a business strategy is now 'normal' and almost universally accepted as such by farmers. Indeed we would suggest that the characteristic resistance to innovation in the early stages of the adoption process has long since passed. Instead we are now perhaps in the phase of late or laggardly adoption. The problem is we are not dealing here with a single innovation (diversification) of universal applicability. On the contrary, we are dealing with a myriad of innovations, only loosely characterised under a single collective heading. In nearly every case these are innovations relevant to highly specific and limited markets, which could not possibly be relevant to more than a minority of

farmers. Thus there is a danger that a combination of diversification having become the norm and the current challenging economic circumstances facing the agricultural industry will prompt some farmers to make the wrong business decisions. Consequently, in policy terms it is important that the signal sent out to farmers is that they should scrutinise their business in the round, rather than adopt any particular strategy. This has major implications for the provision of sound and independent advice tailored to the individual circumstances of farm businesses. Our research also demonstrated the wide-ranging levels of financial performance within the various diversified enterprises. This also needs to be understood and taken into account within farm business advisory services. In contrast to mainstream commodity production, well catered for in terms of financial data by the Farm Business Survey, we doubt that many private or public-sector advisors and consultants have access to adequate benchmarking data for many diversified enterprises.

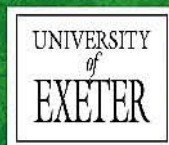
Furthermore, the current drive to develop collaborative marketing groups and co-operatives in order to share costs, secure professional marketing expertise and operate on a scale to support larger marketing and processing activity may also be as relevant to diversified enterprises as to mainstream commodity production.

The second social issue we wish to highlight is that the changing relative importance of diversified enterprises within the farm business as a whole has had social ramifications within farm households. This is particularly the case where female or junior members of the household are now involved in diversified enterprises which now provide the majority of household income. There may also be implications for countryside management as this shift in balance occurs. Thus the growth of diversification may also lend further weight increase to the widely accepted view that the key to achieving a sustainable future for rural economies is dealing with the issues and potential solutions in a more integrated way. As Midmore et al (1998) argue for the uplands, 'in order to attain a more sustainable rural economy .... an approach that integrates emerging consumer trends, farming community involvement, research and education in a self-contained package is essential.'

Finally we turn to research requirements. We recommend that future research should concentrate on the following key issues:

- The provision of regular and up-dated benchmarking data on a range of key diversified enterprises, possibly obtained through bolt-on studies to the Farm Business Survey, or as ancillary components of the survey itself.
- The need to explore in greater detail the transition from primarily agricultural businesses to primarily diversified businesses in terms of social and environmental implications.
- The implications of growing farm diversification for knowledge transfer activities.
- The need for revisions to both the agricultural census and the Farm Business Survey to deal with diversified enterprises.
- The growing complexity of family, business and farming inter-relations, including the growth of new forms of business structure.





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