

Farmland Booms and Busts: Will the Cycle be Broken?

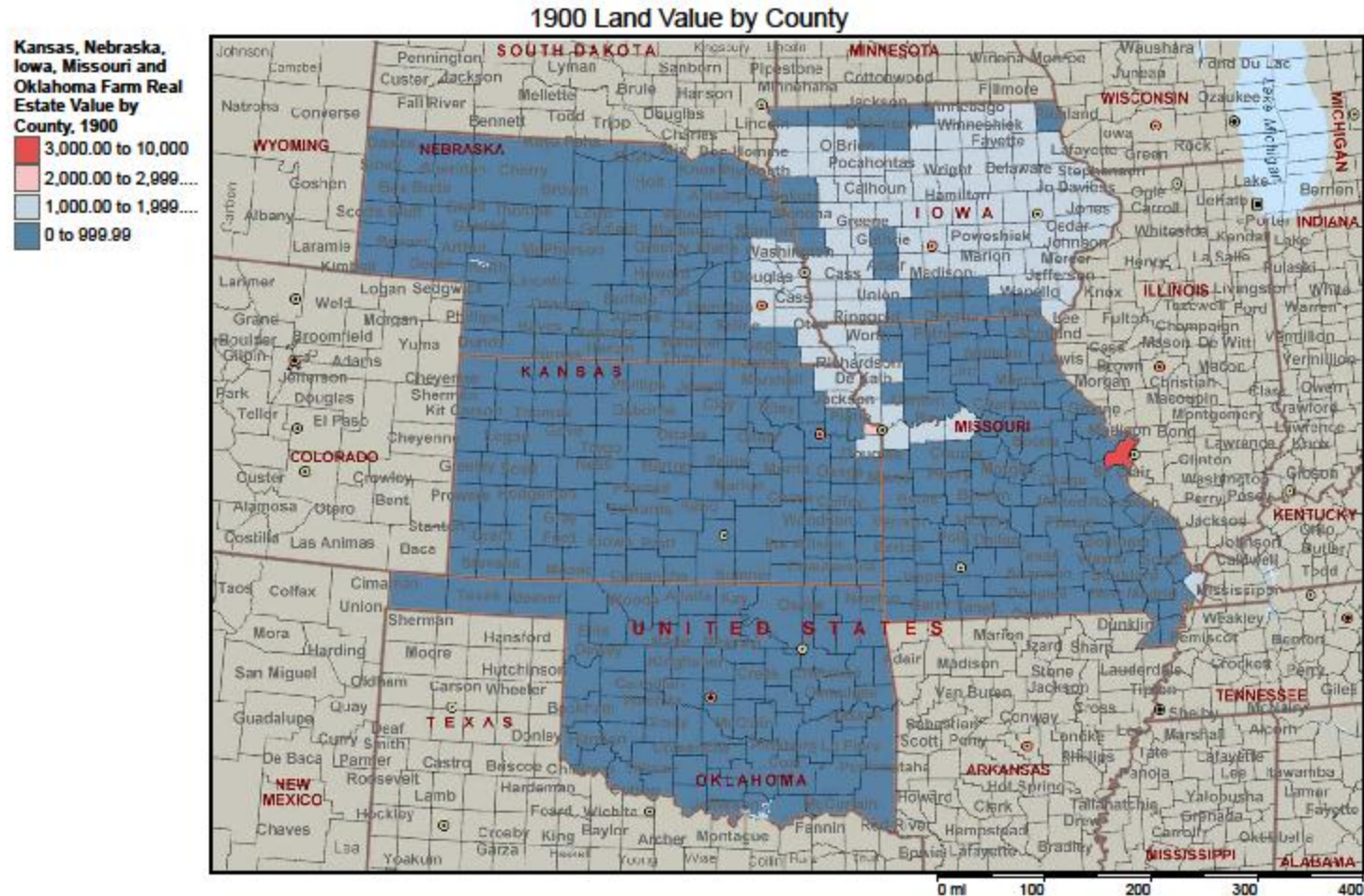
Kansas Society of Farm Managers and Rural Appraisers
Salina, KS
February 23rd, 2012

Brian C. Briggeman
Associate Professor and
Director of the Arthur Capper Cooperative Center

KANSAS STATE
UNIVERSITY

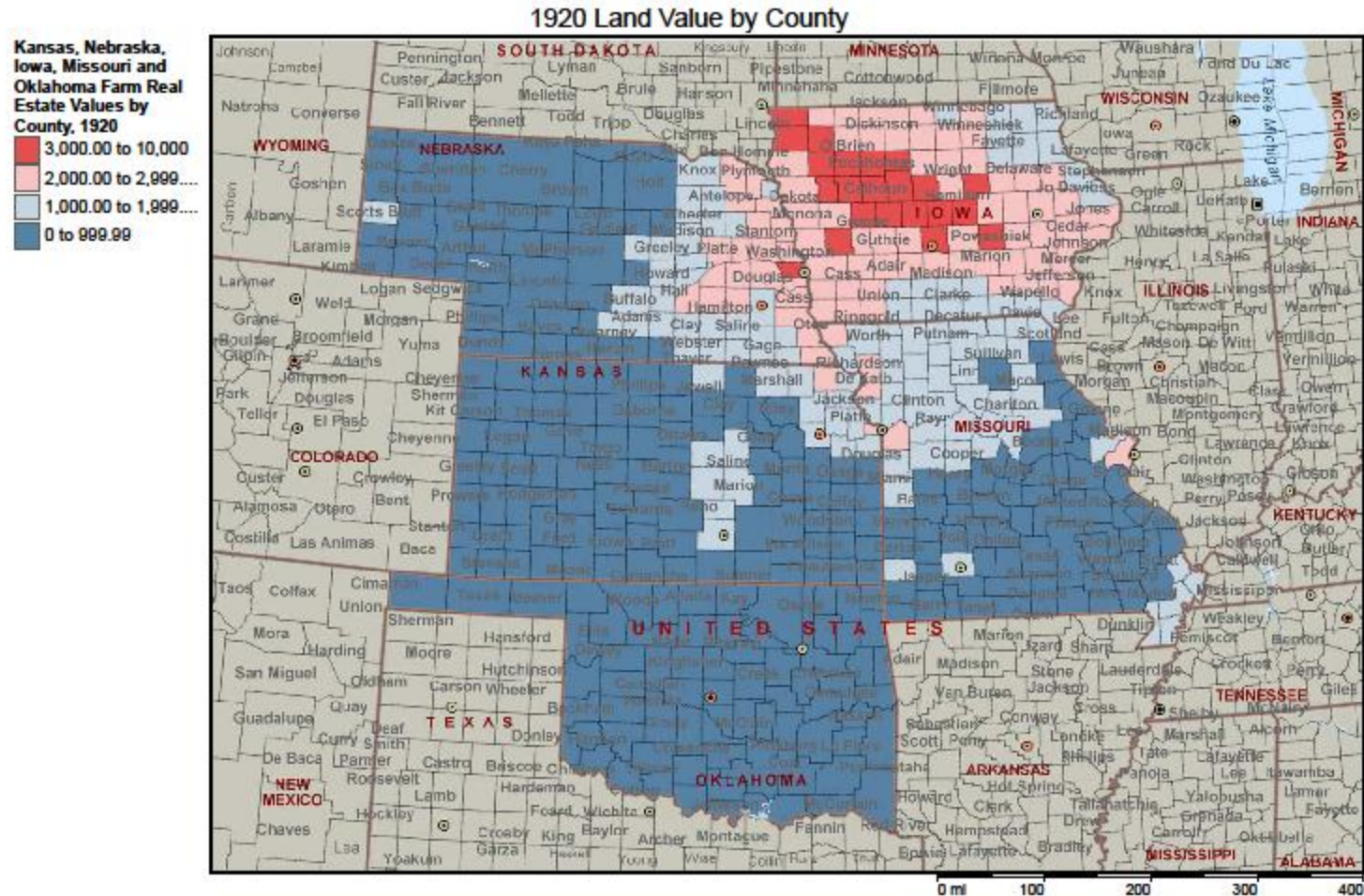
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With the start of the 20th century, farmland values began to heat up.



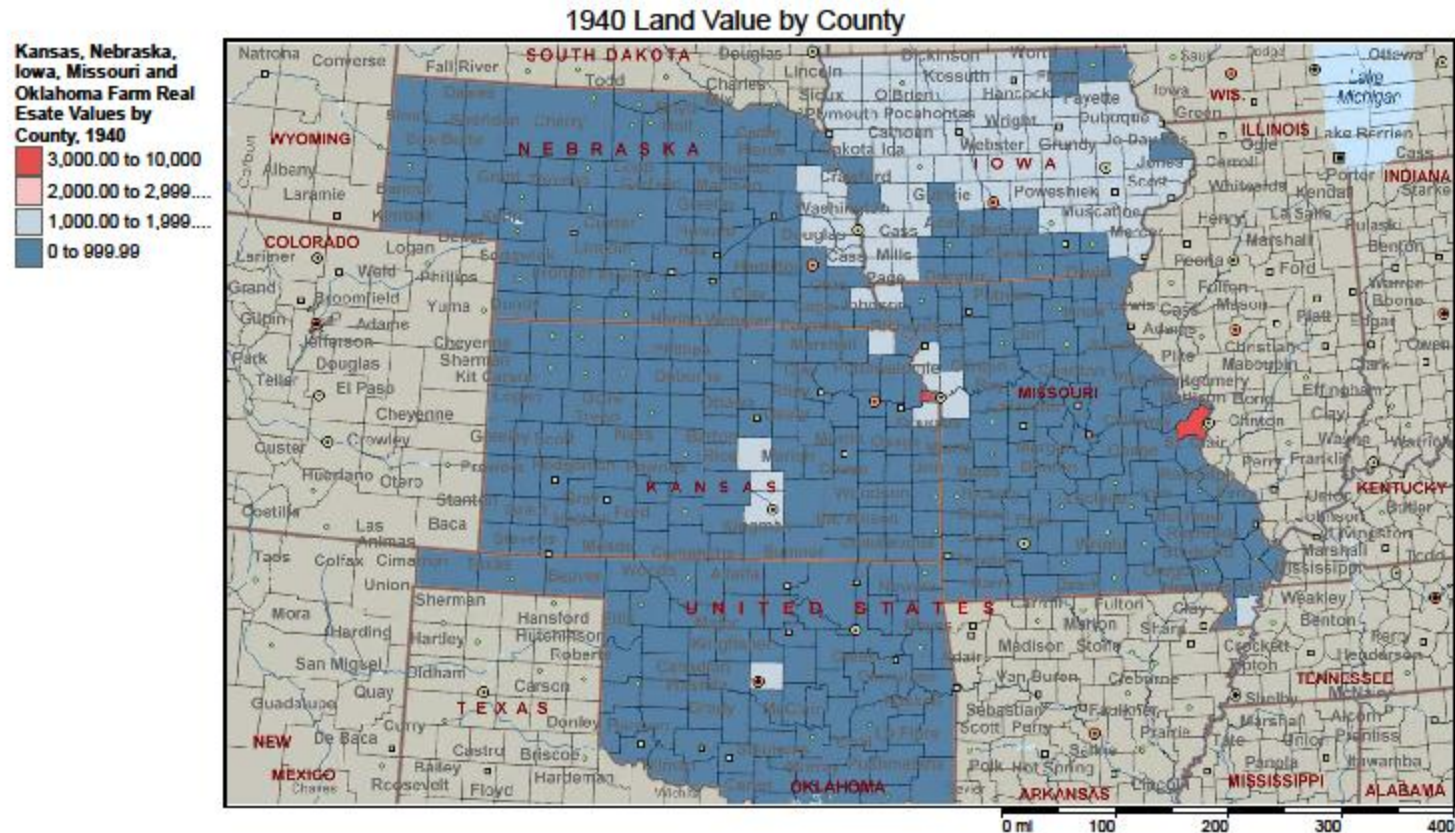
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After World War I, farmland values caught “fire” with surging ag exports and excessively leveraged farms.



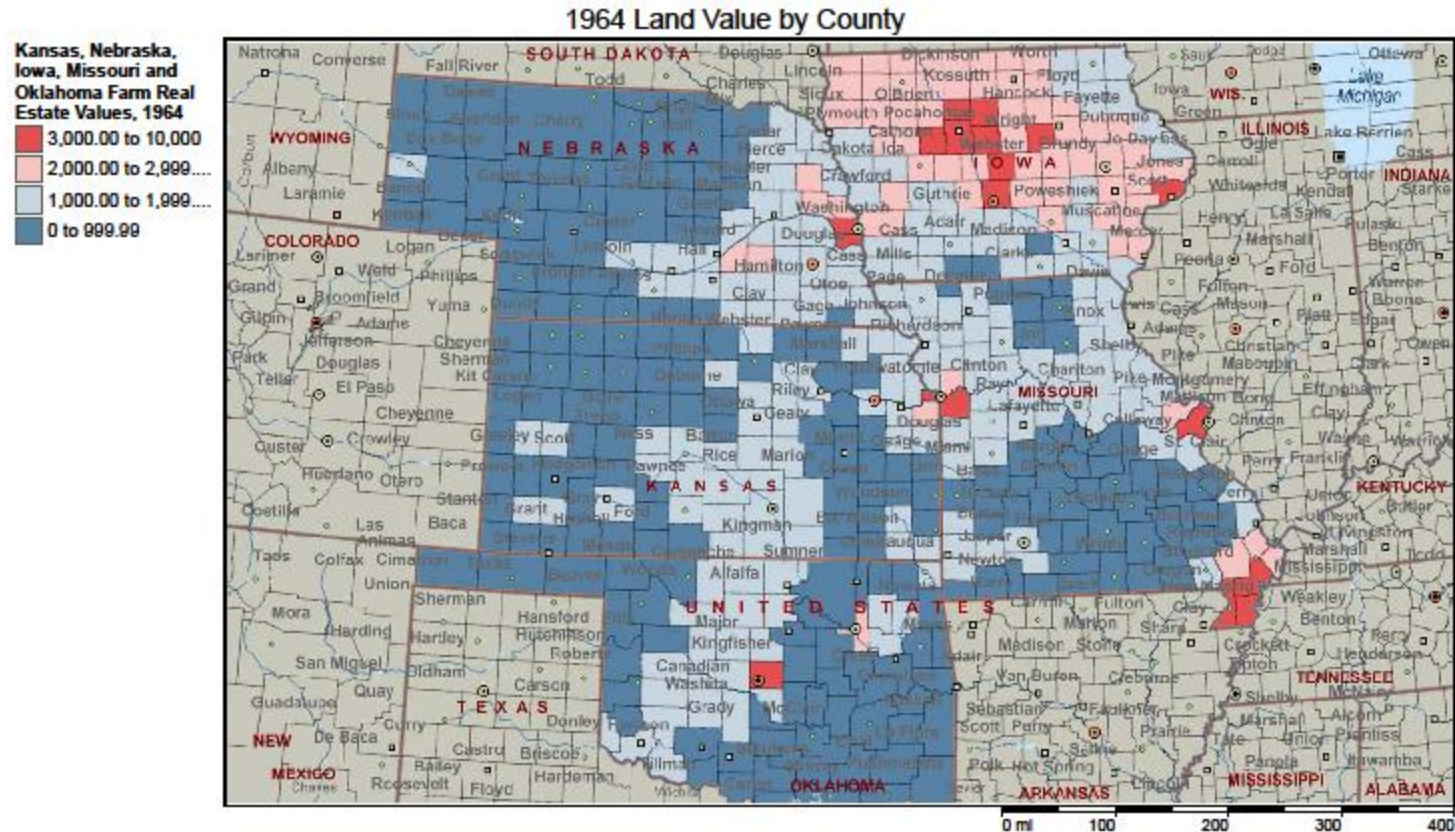
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After a surge in bankruptcies and the Great Depression, the “fire” was out.



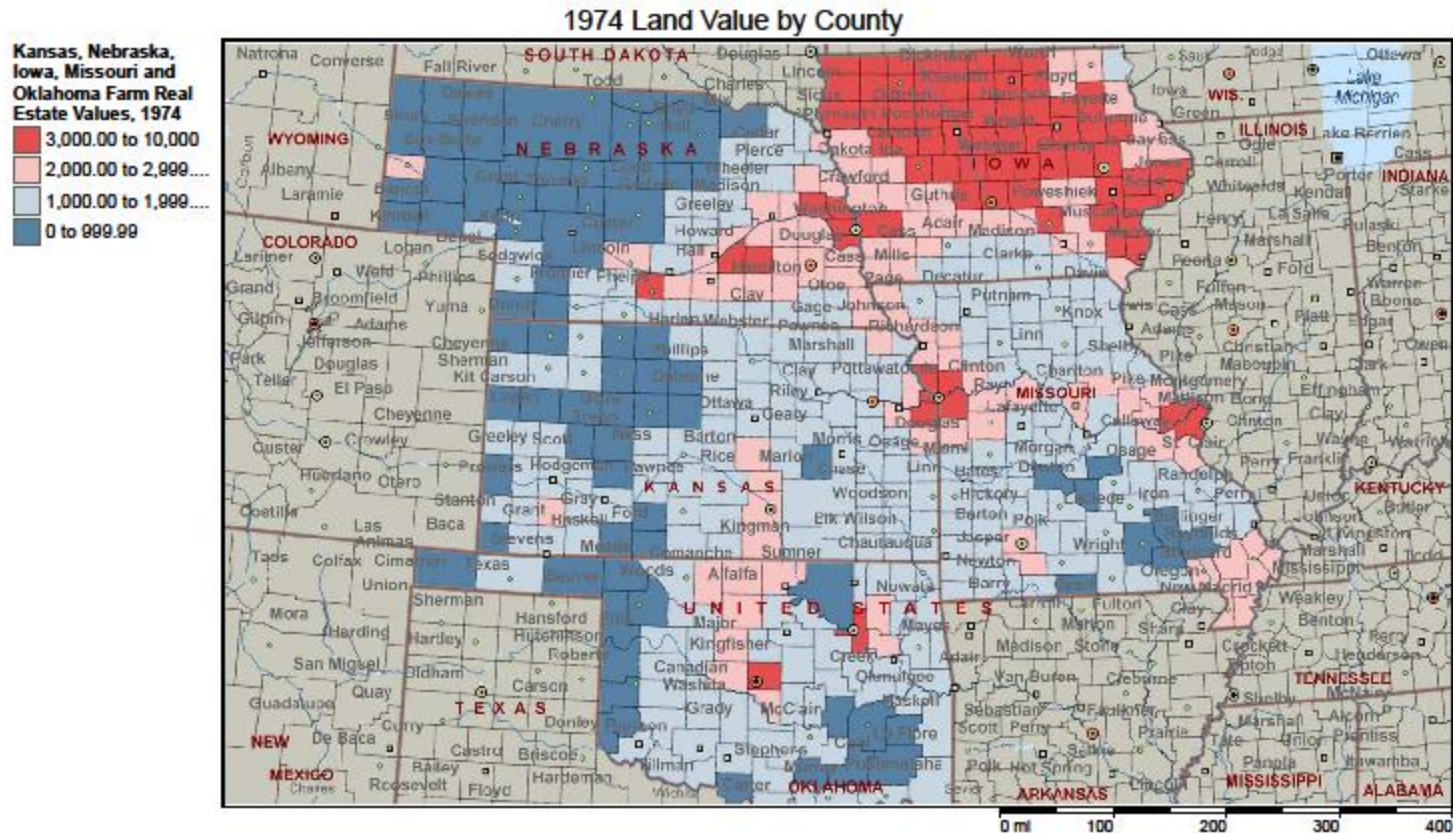
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After World War II, farmland values started to heat up again as new technology was adopted.



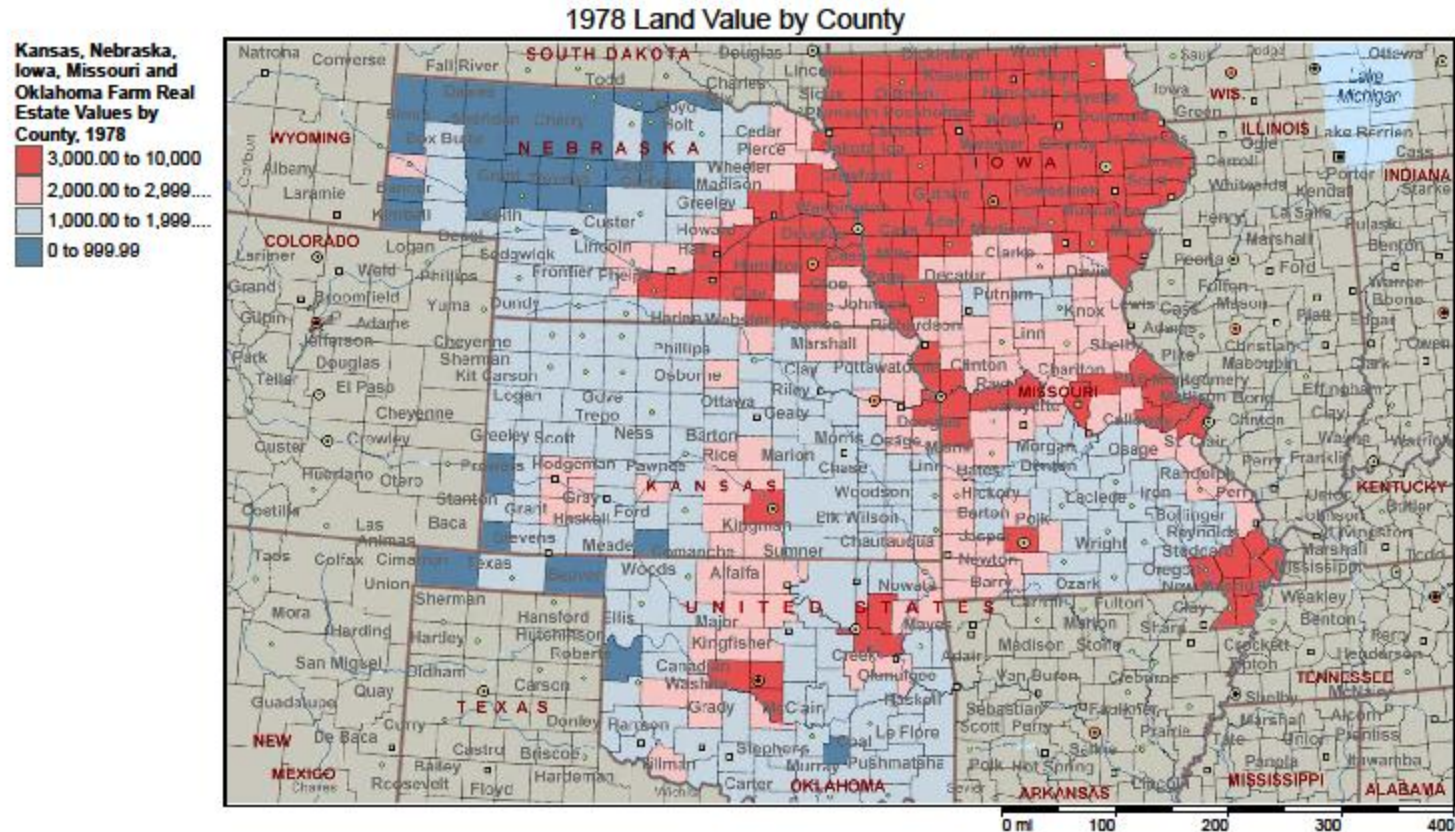
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New export markets and easy credit set farmland values ablaze, especially in the corn belt.



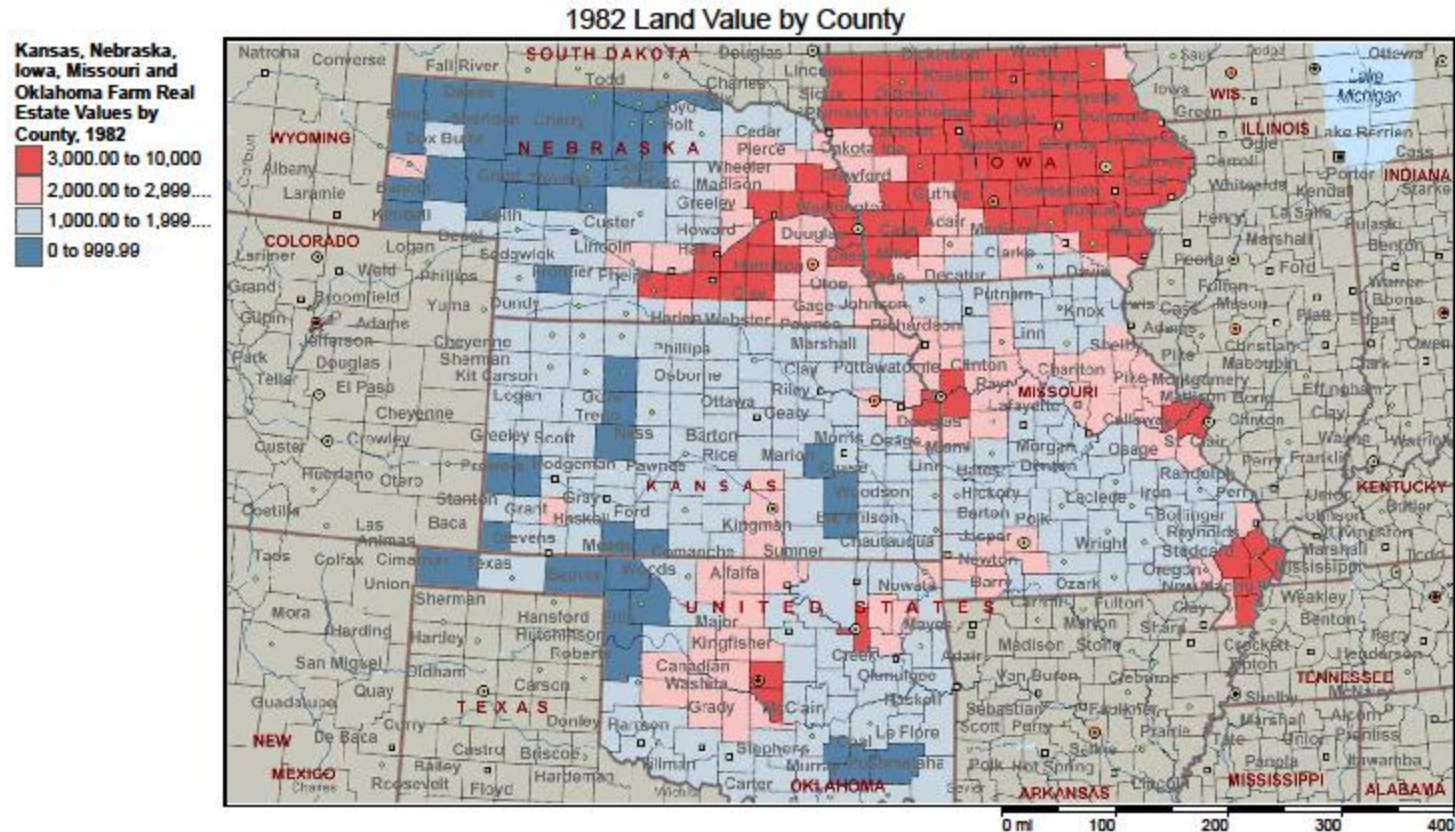
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By 1978, Iowa farmland values were “red hot” and it was spreading throughout the region.



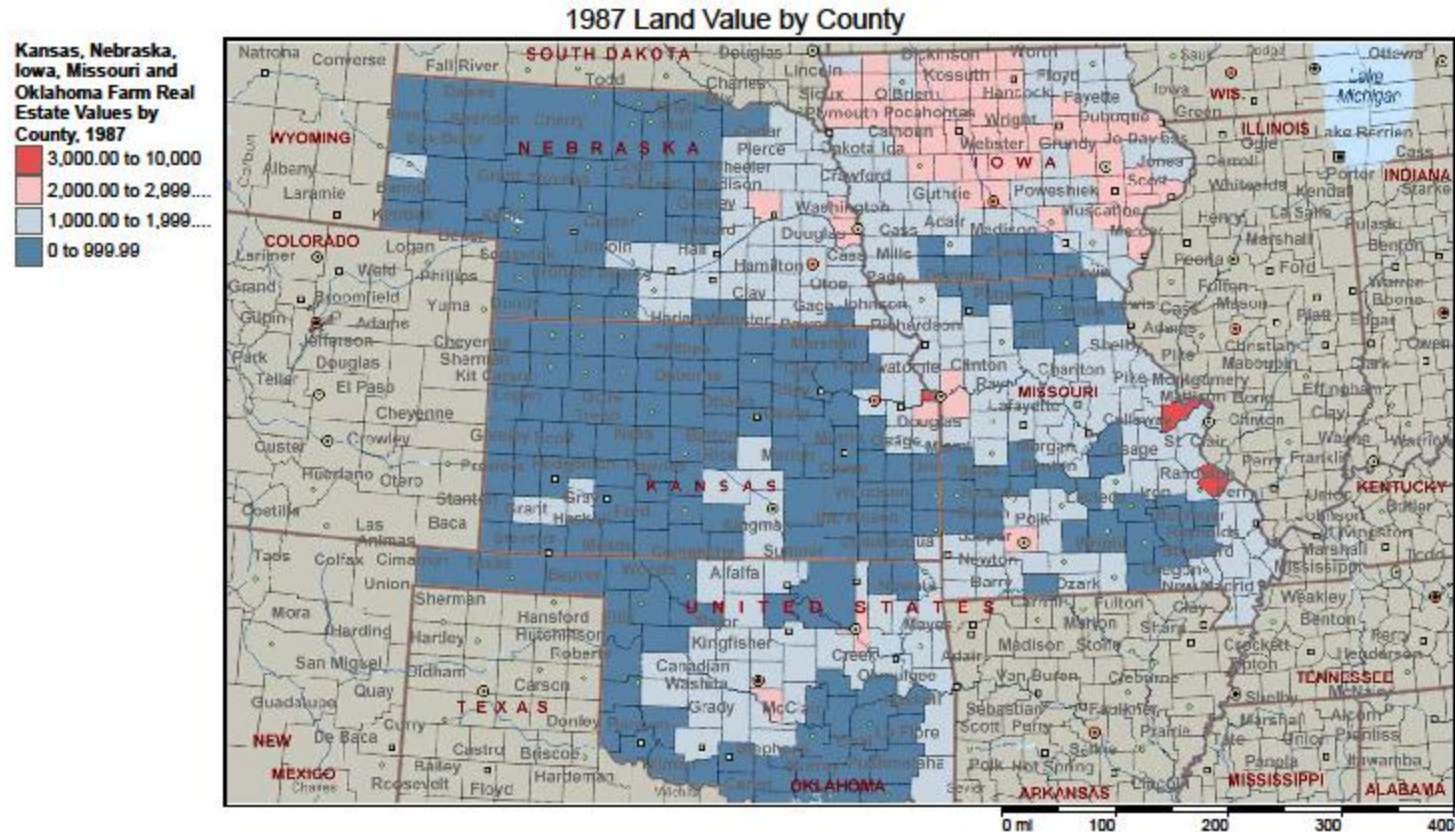
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The start of the 1980s farm debt crisis began to cool the flame surrounding farmland values.



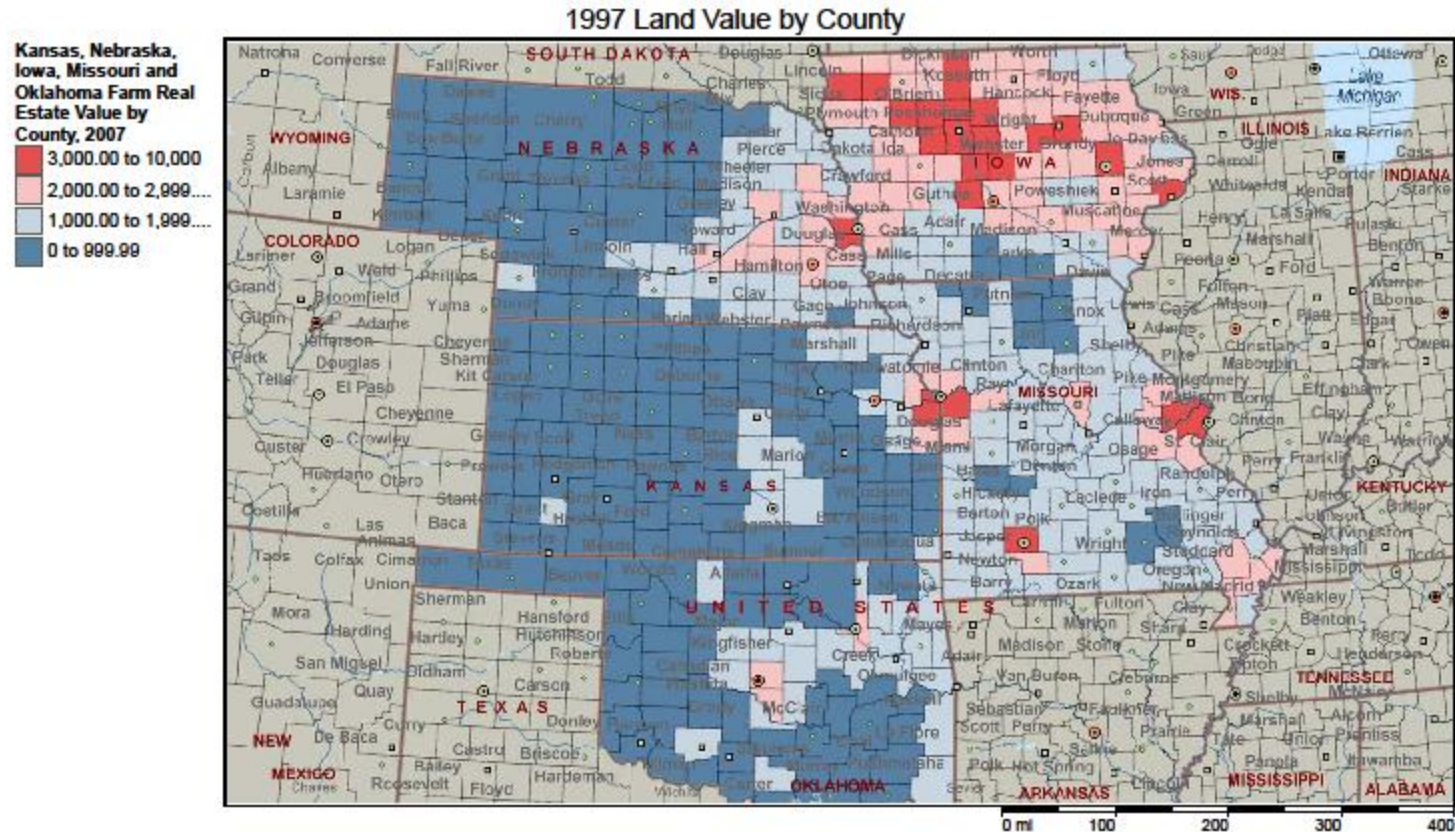
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By 1987, forced land sales and a collapse in farm income put the “fire” out.



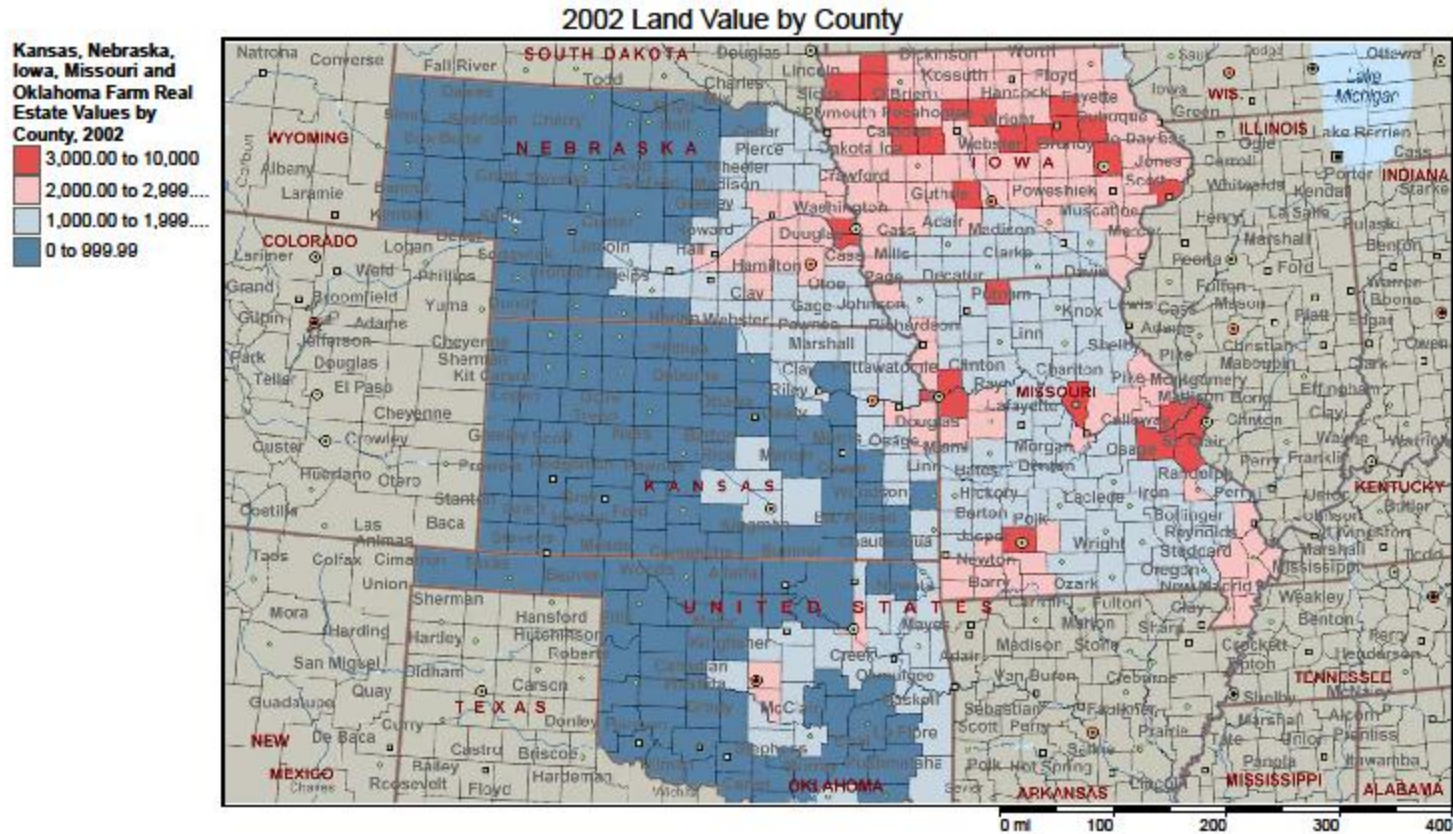
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After the 1980s, a slow, steady recovery helped farmland values recover.



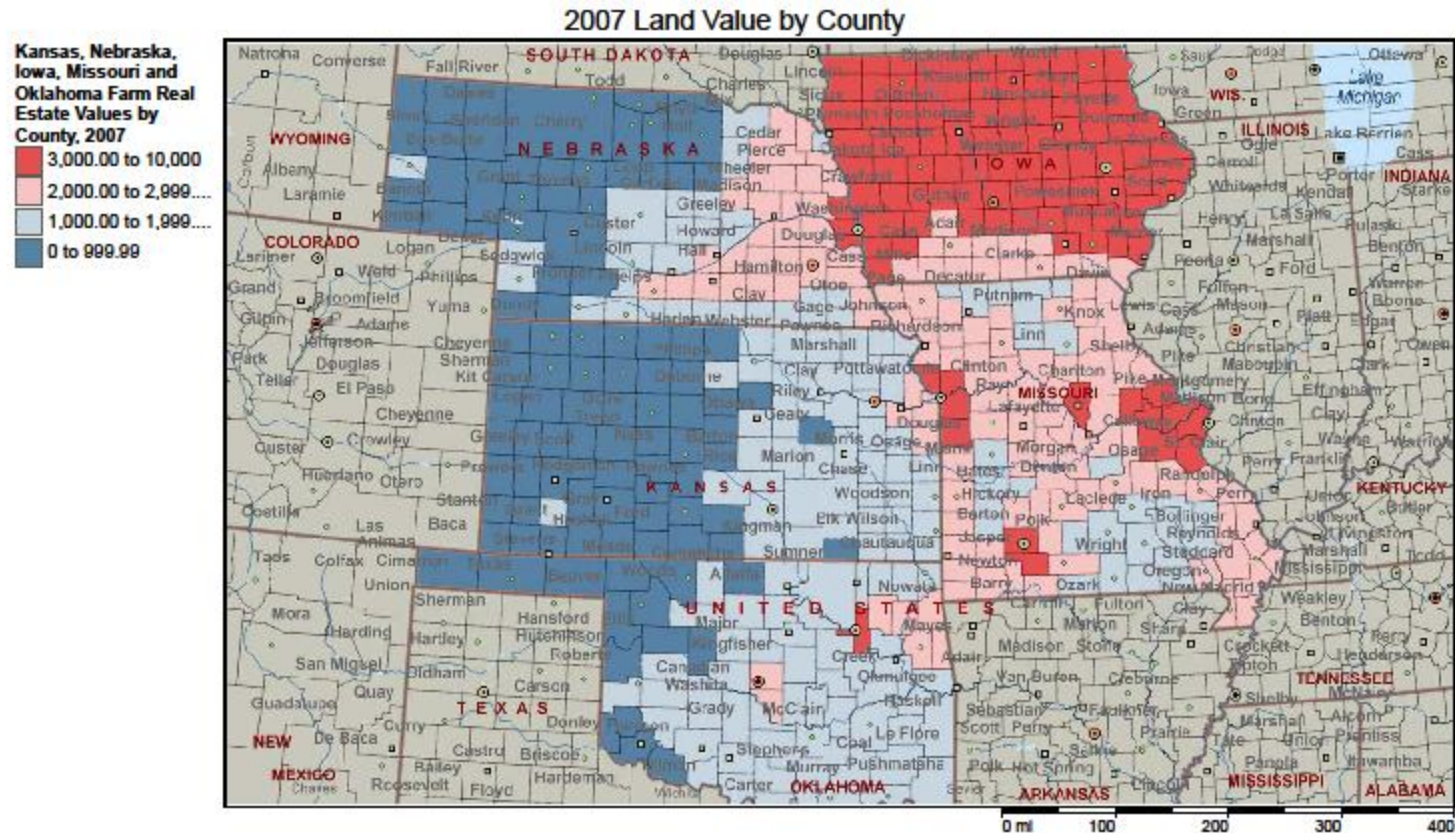
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At the turn of the century, farmland values held steady until...



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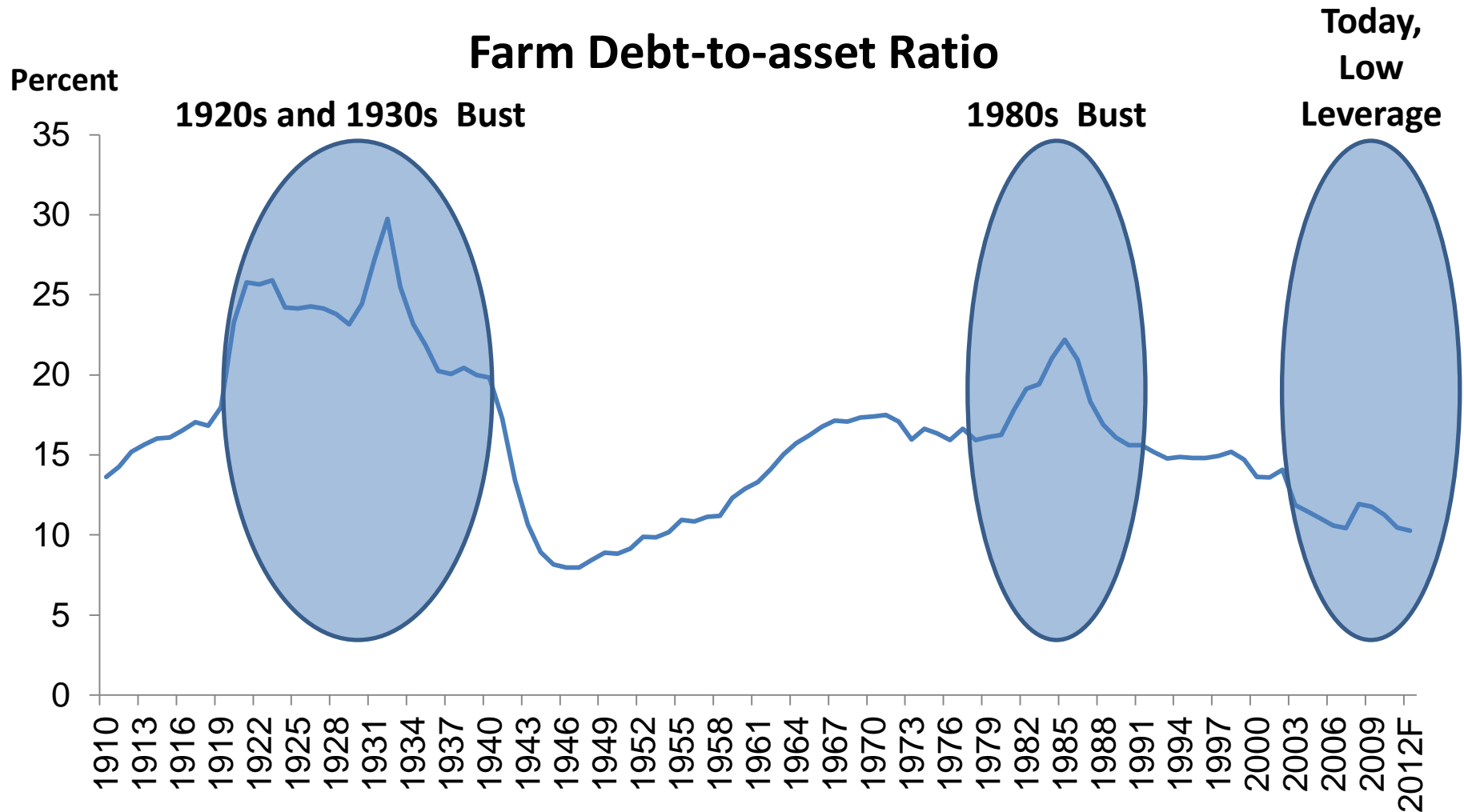
...a booming U.S. housing market as well as surging ag exports lit another “fire” under land values.



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**EXCESSIVE LEVERAGE PLAYED A
SIGNIFICANT ROLE IN THE TWO
FARMLAND VALUE COLLAPSES DURING
THE 20TH CENTURY...TODAY?**

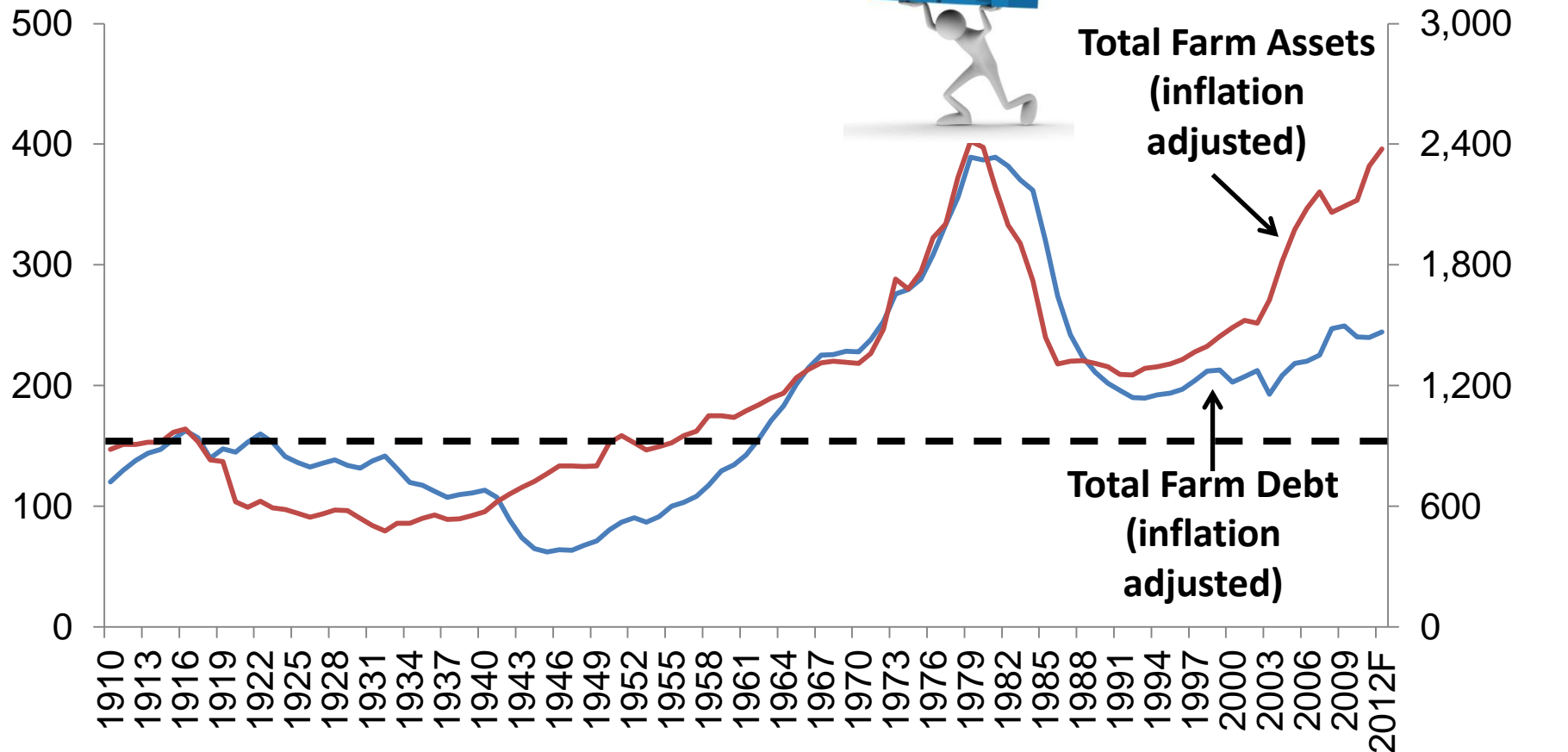
Debt-to-asset ratios rose significantly during the 1920s and 1980s.



Source: Agricultural Finance Databook (1910-1959), USDA (1960-2012F)

With “easy” credit, real farm debt levels and asset levels surged in the 1970s.

Constant 2010
Billion Dollars



Source: Agricultural Finance Databook (1910-1959), USDA (1960-2012F)

Today, leverage in the farm sector is low...farmland bust?

 **REUTERS**

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FDIC chair warns of possible US farmland 'bubble'

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*** Says U.S. farmland values requires "close monitoring."**

*** Farmland values 58 percent above 2000 levels**

By [Carey Gillam](#)

KANSAS CITY, Mo., Oct 18 (Reuters) - U.S. farmland could be the next asset bubble at risk for bursting, a leading banking regulator said on Monday.

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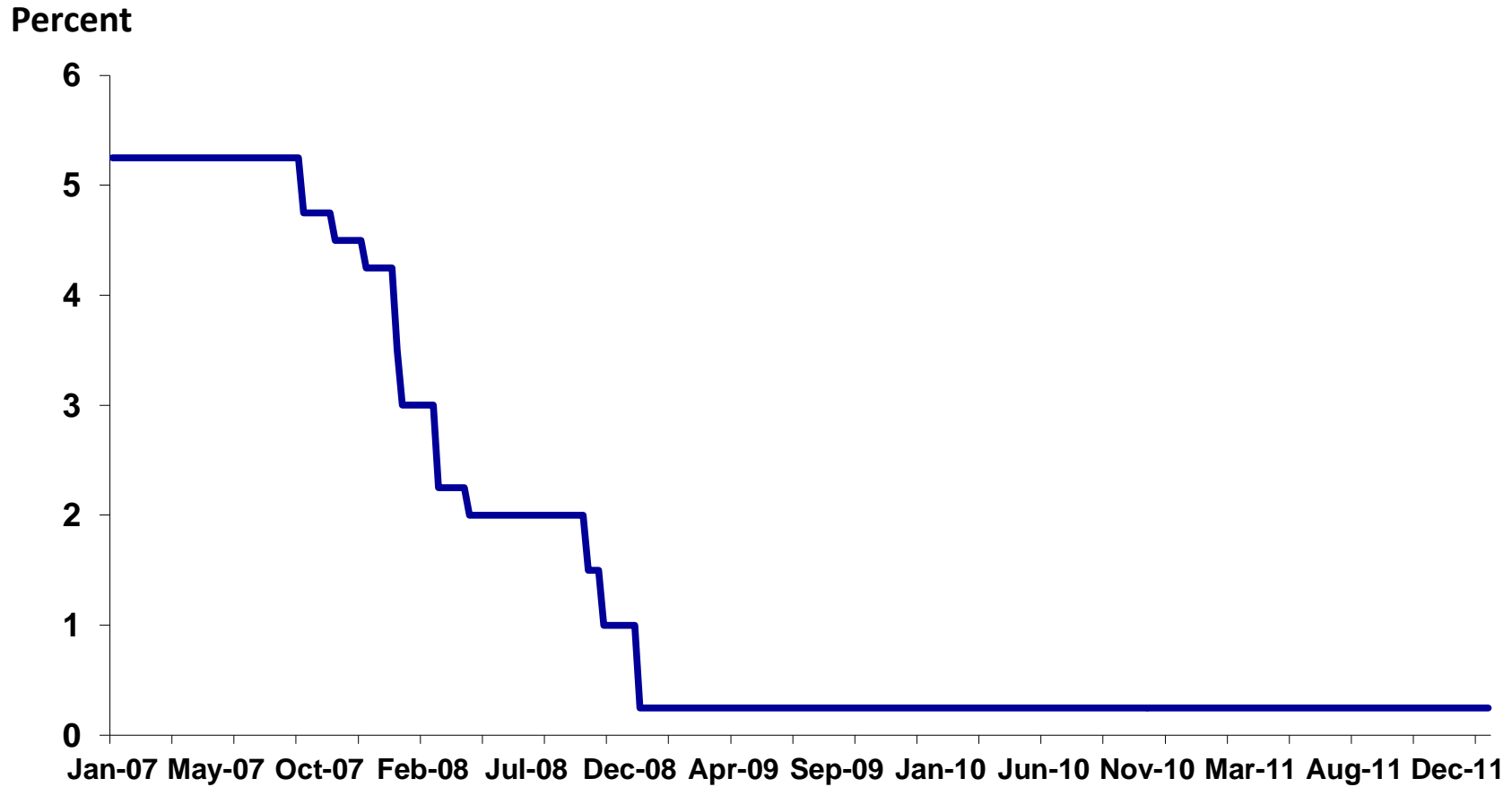
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Ultra low interest rates are one reason why regulators are warning of a farmland bubble.

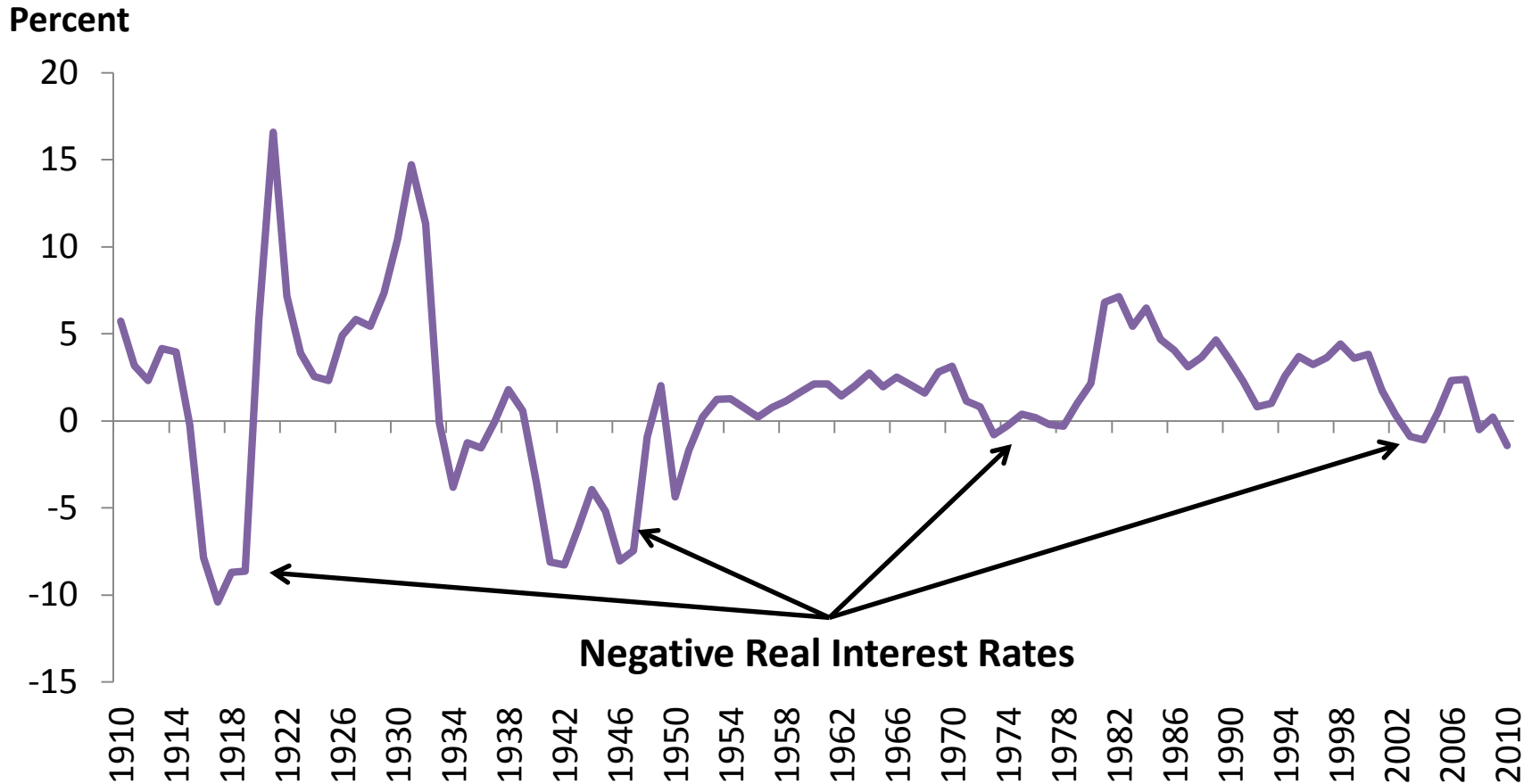
Fed Funds Rate (Upper Bound)



Source: Federal Reserve Board of Governors

Movements in real interest rates also play a role in the farmland market... opportunity cost.

Real Commercial Paper Rates



Source: Featherstone, Allen M. and Timothy G. Baker. 1987. "An Examination of Farm Sector Real Asset Dynamics: 1910 – 85." American Journal of Agricultural Economics 69(3): 532-546, and Federal Reserve Board of Governors

Iowa: Bidders Vie for Bragging Rights at Cash Rent Auctions

AgFax.Com - Your Online Ag News Source

By Elizabeth Williams, DTN/Telvent

Nearly 300 people crammed into a motel meeting room to attend the first cash rent public auction in the Mason City, Iowa, area last Saturday, Feb. 4. About 25 active bidders raised hands or nodded heads as two-year leases for more than 2,250 tillable corn/soybean acres in 14 tracts went up for grabs. After the final “going once, twice, sold,” the tillable-acre winning bids ranged from a low of \$325 for 78 acres (62 tillable, subject to flooding) to \$520 for 108 acres (all tillable).

Most of the winning bids ranged from \$425 an acre to \$490 per tillable acre, rates that left onlookers somewhat stunned. After all, farmers in Iowa’s most expensive cash rent county only paid an average of \$235 an acre in 2011, according to USDA. The excessive rent also means growers will be shouldering sizable risk should commodity prices plunge to more normal levels between now and 2014 and probably dictates that corn will be the crop of choice to pay the bills on that land.

The Mason City event was the fourth cash land lease auction in three days for the owners, Charles E. Lakin Enterprises out of Omaha, a family business enterprise that had expiring leases on 3,336 tillable acres in Iowa. The Lakins’ farms are scattered over eight counties in western, central and north central Iowa.

“We weren’t sure what the cash rent market was and we didn’t know how to set a fair price, so we thought we’d try an auction,” said Chuck Lakin, son of Charles E. Lakin. “It worked out pretty well.”

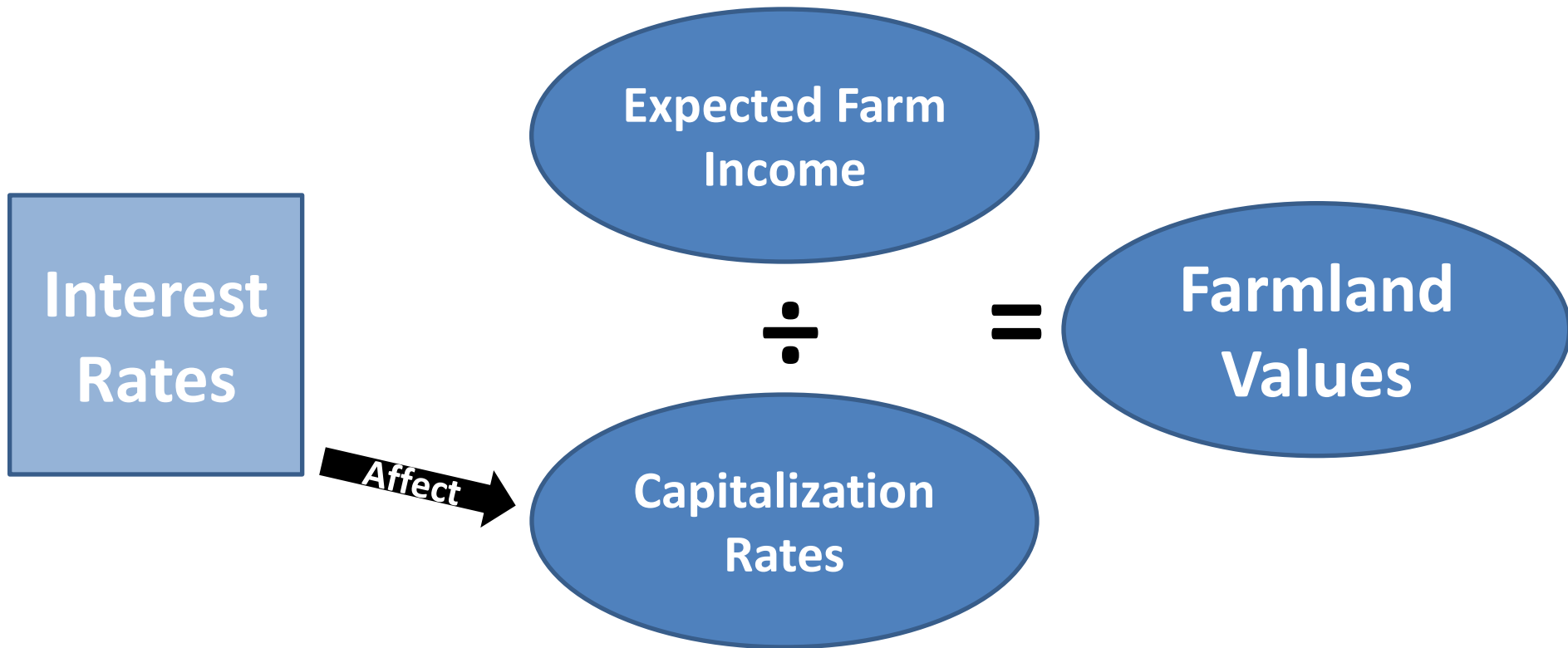
Farmland tenants generally dislike public lease auctions for two reasons: 1) They remove the traditional, personal relationship bond between the owner/tenant and reduce it to a numbers game; and 2) It publicizes actual cash rents so all the landlords in the area can compare how their leases stack up. Even if you are the highest bidder and get the ground, you may not want your other landlords to know you are willing to pay that much for land. In fact, one of the current tenants (who won the highest bid on ground he had been farming) had a proxy at the Lakin farm lease auction and came in after the auction to sign the papers and write the check.

For the landowner, an auction “takes away the stress from negotiating with the tenant and gives the land the potential to reach its fair market value,” said Allan Hughes who conducted the Lakins’ lease auction.

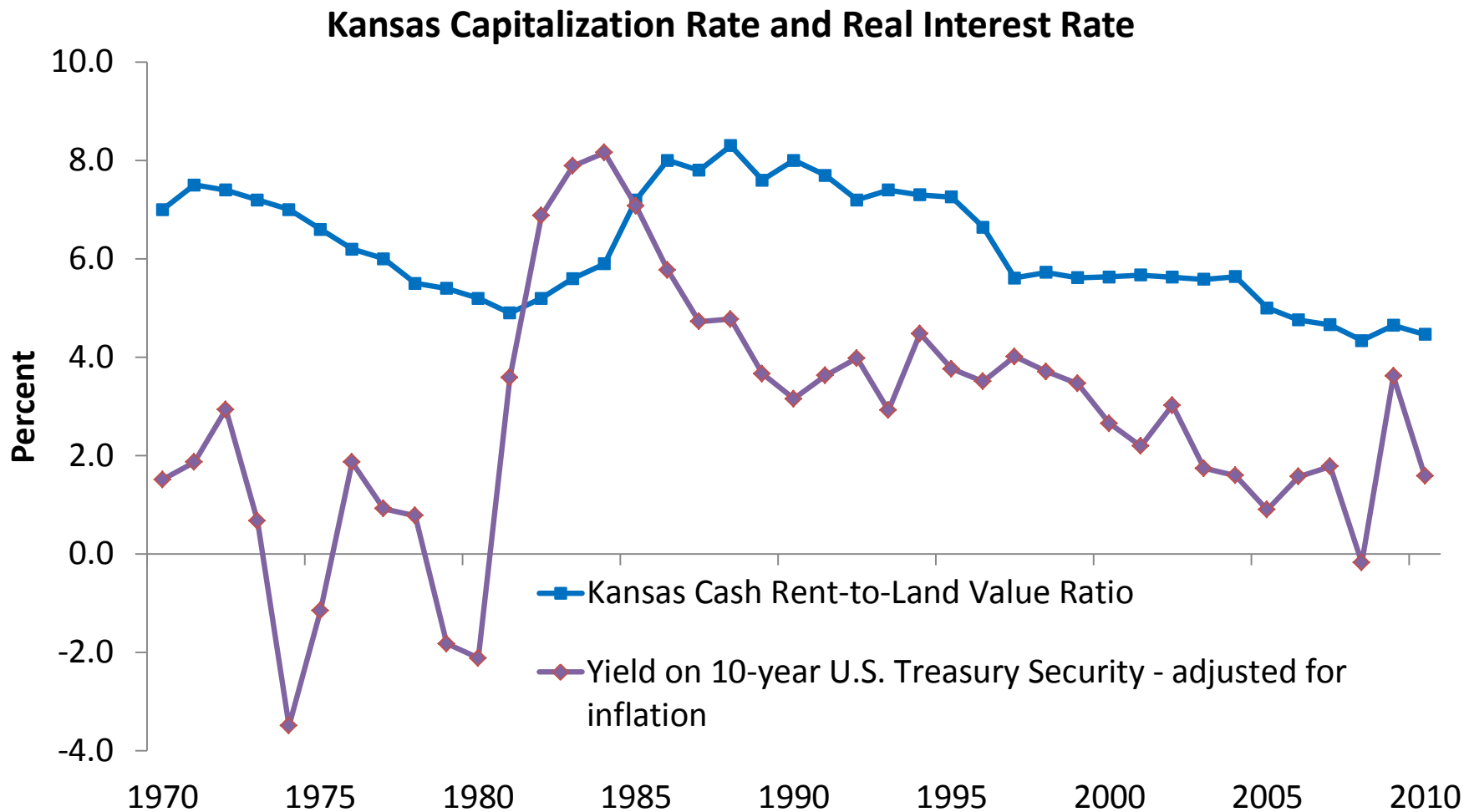
“These leases are structured so good husbandry is required,” explained Hughes. A five-page lease requires the tenant to keep the ditches free and clear and to provide soil tests, fertility input records, yield information on each farm.

Low winning auction bid, \$325/acre (subject to flooding)
High winning auction bid, \$520/acre

While debt is not fueling the recent surge in farmland values today, ultra low interest rates are playing a significant role.

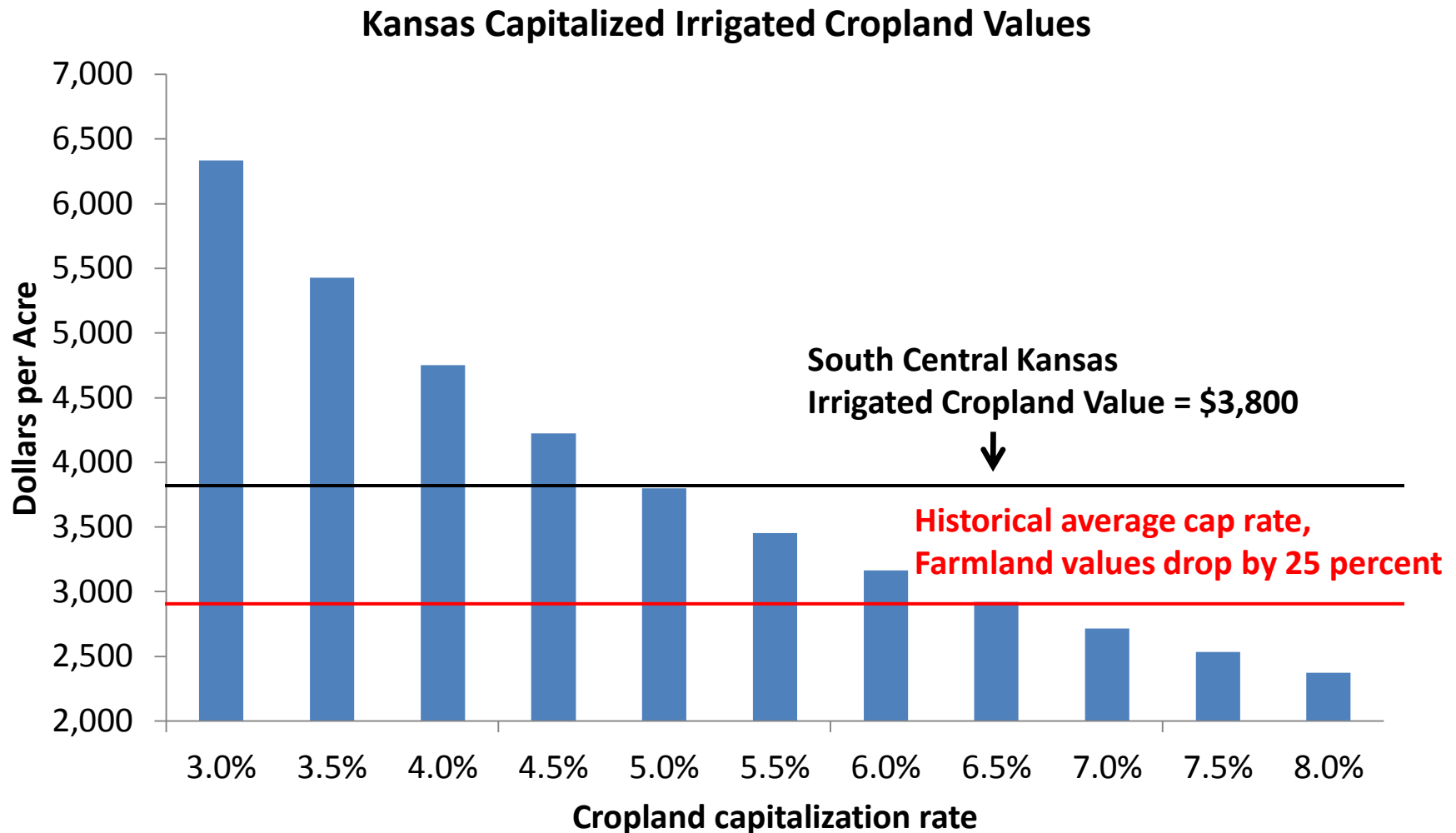


Capitalization rates and real interest rates tend to move together.



Sources: USDA , Federal Reserve and BLS

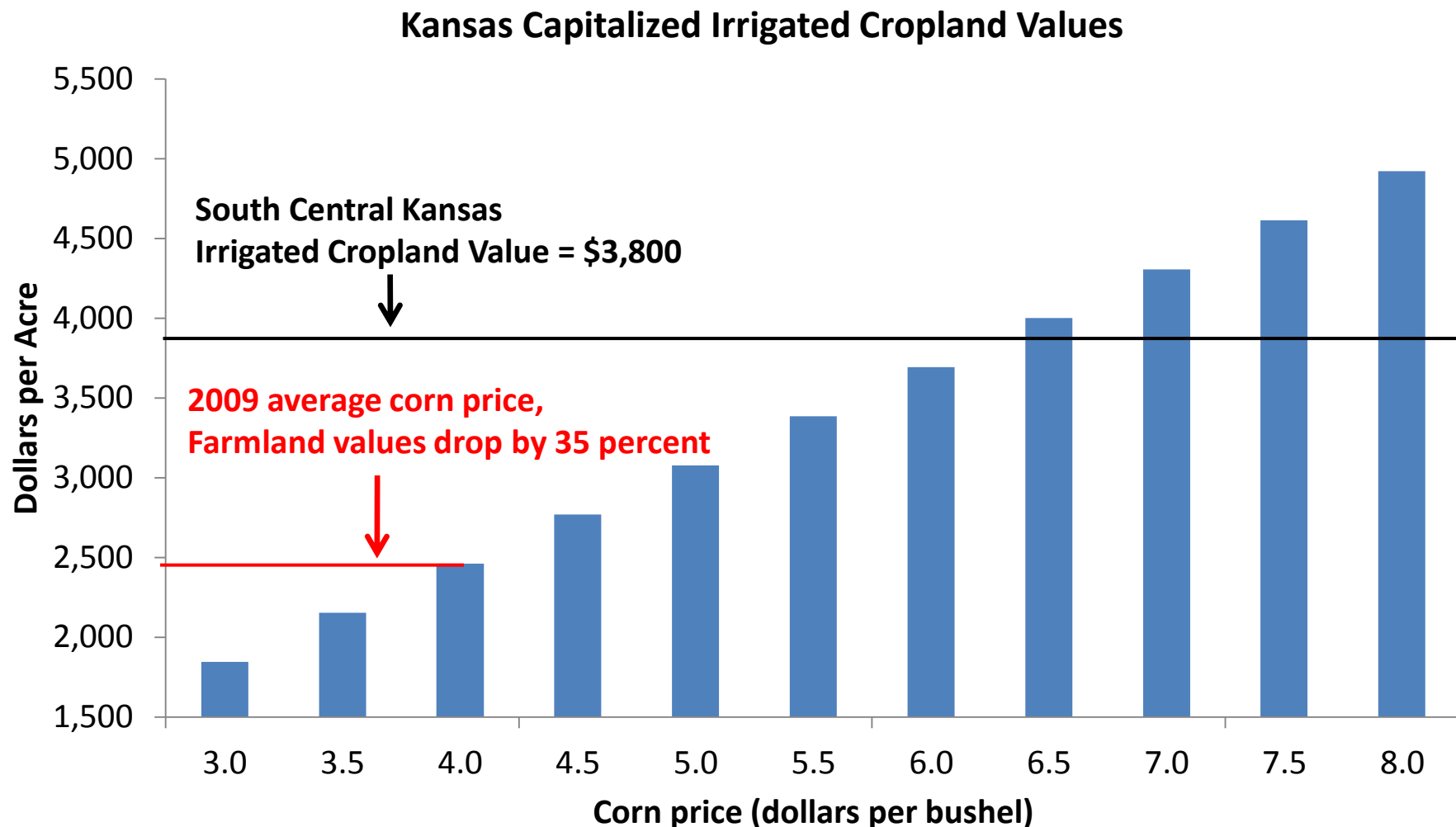
Historically low capitalization rates help support current Kansas cropland values.



Authors' calculations based on KSU Corn Cost-return Budget in South Central Kansas.

Assumed 200 bushels per acre, a corn price of \$4.75 per bushel, and 20% of gross revenues capitalized into land.

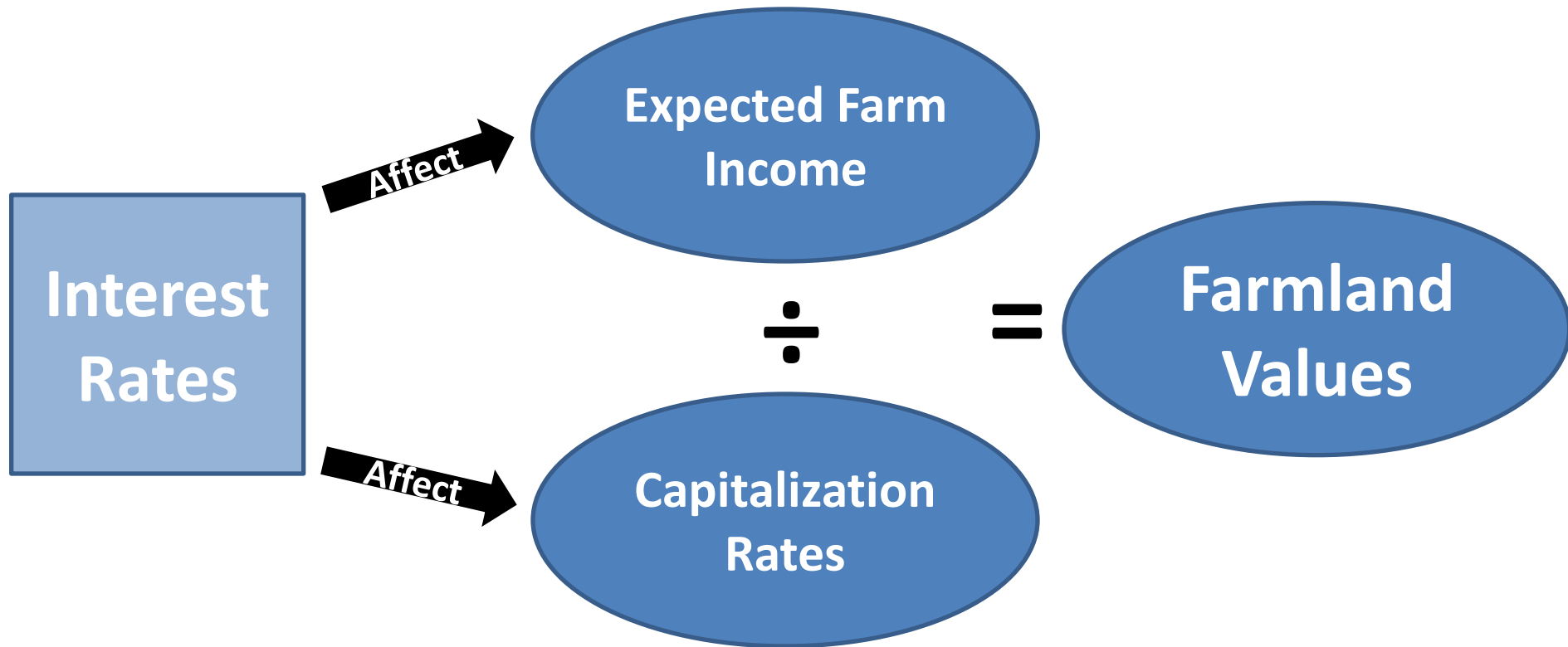
At a historical average cap rate and today's corn prices, current Kansas cropland values are reasonable.



Authors' calculations based on KSU Corn Cost-return Budget in South Central Kansas.

Assumed 200 bushels per acre, a corn price of \$4.75 per bushel, 20% of gross revenues capitalized into land, and cap rate of 6.5%.

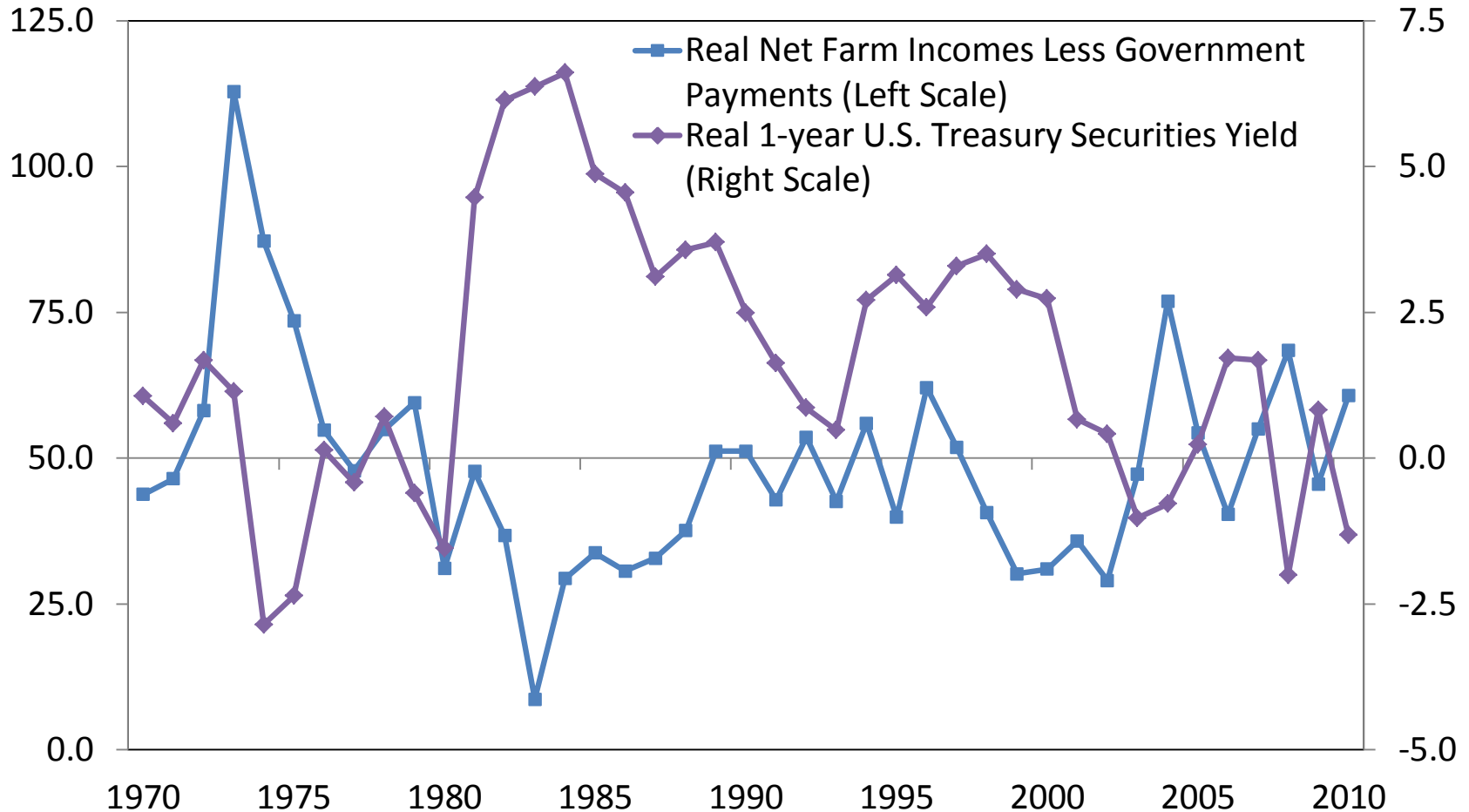
In general, interest rates, through exchange rates, also have an impact on farm income.



Over time, real interest rates and real net farm income tend to move in opposite directions.

Constant 2005 dollars (billions)

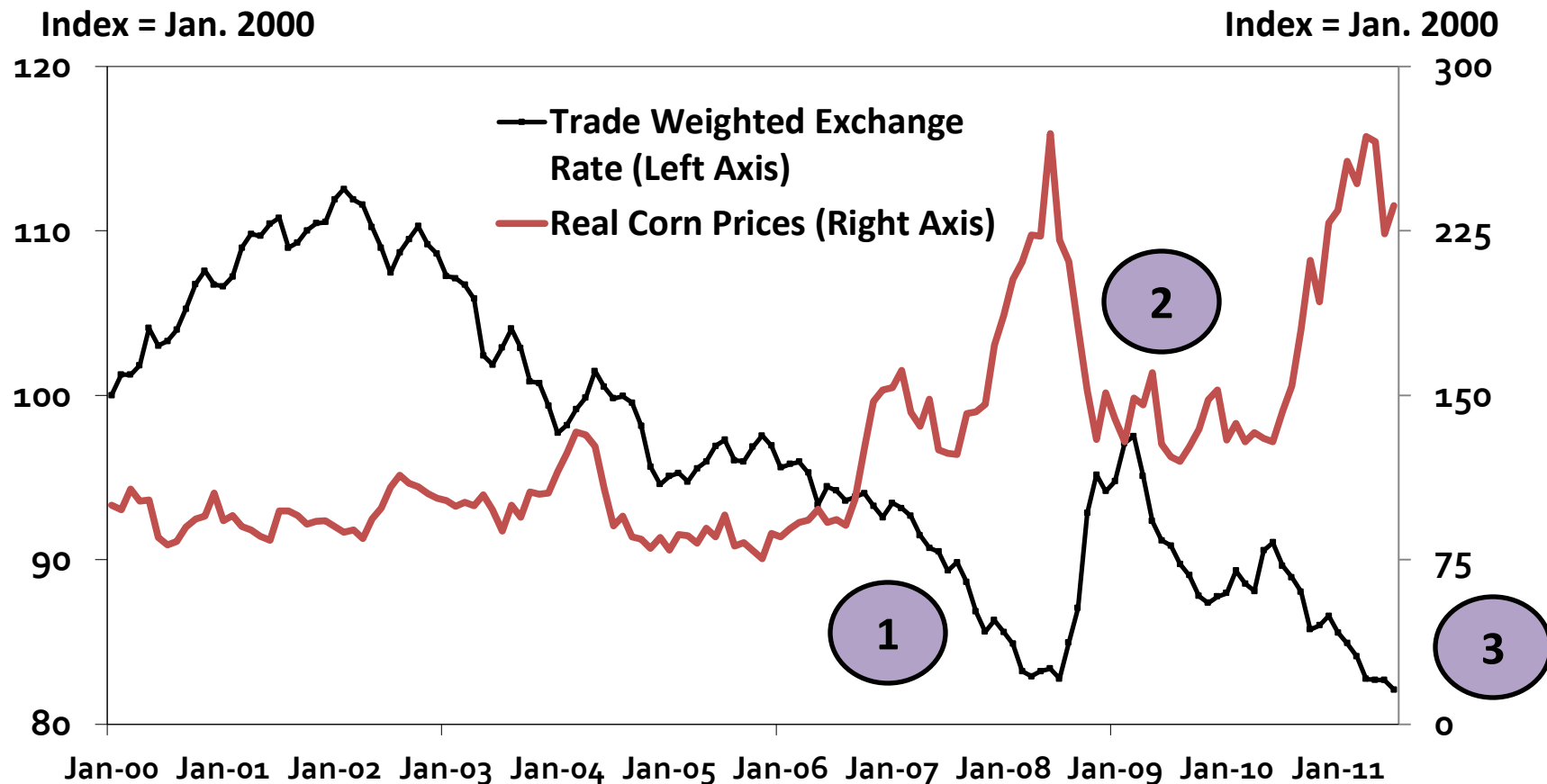
Percent



Sources: USDA , Federal Reserve, BLS

If financial market stress were to rise, how might crop prices respond?

Exchange Rate and Corn Price Indices

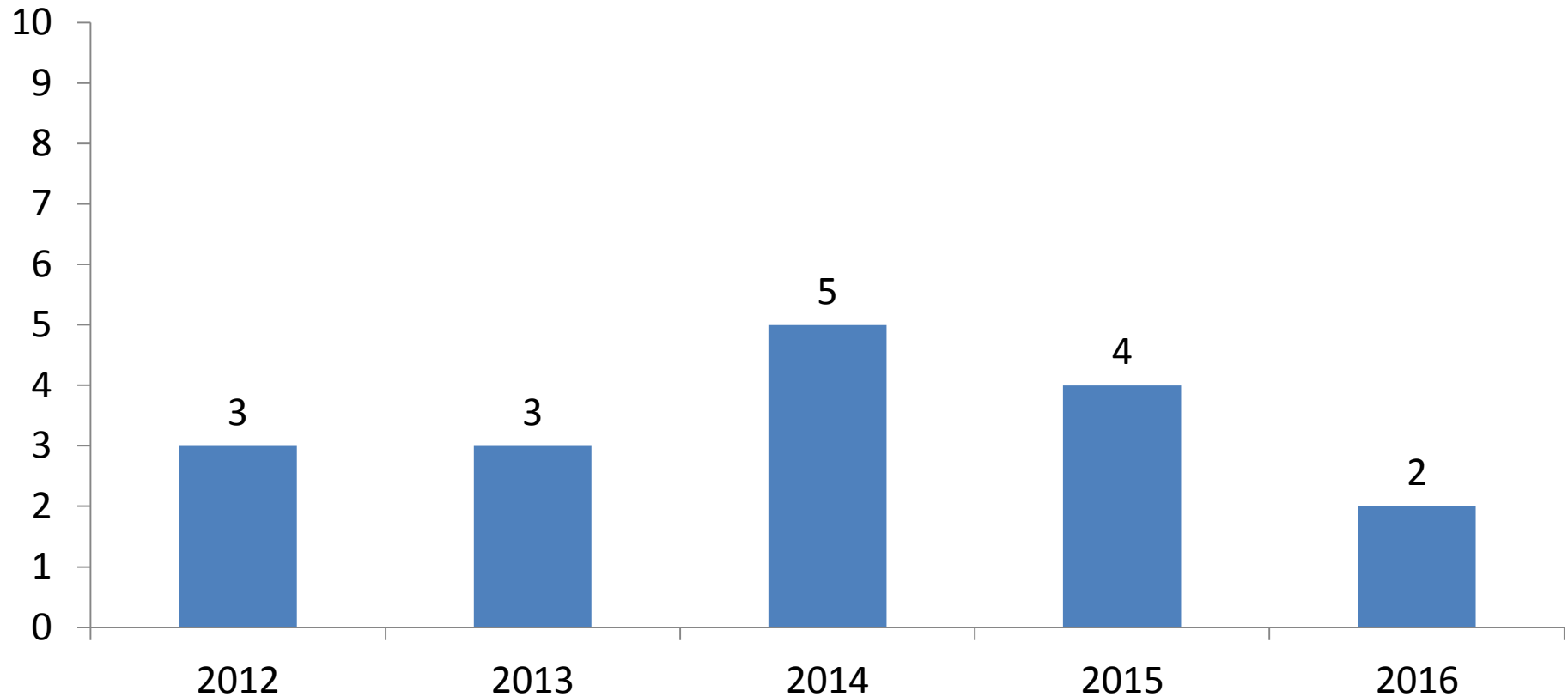


Source: Federal Reserve Board of Governors and Chicago Board of Trade

WHEN MIGHT INTEREST RATES RISE?

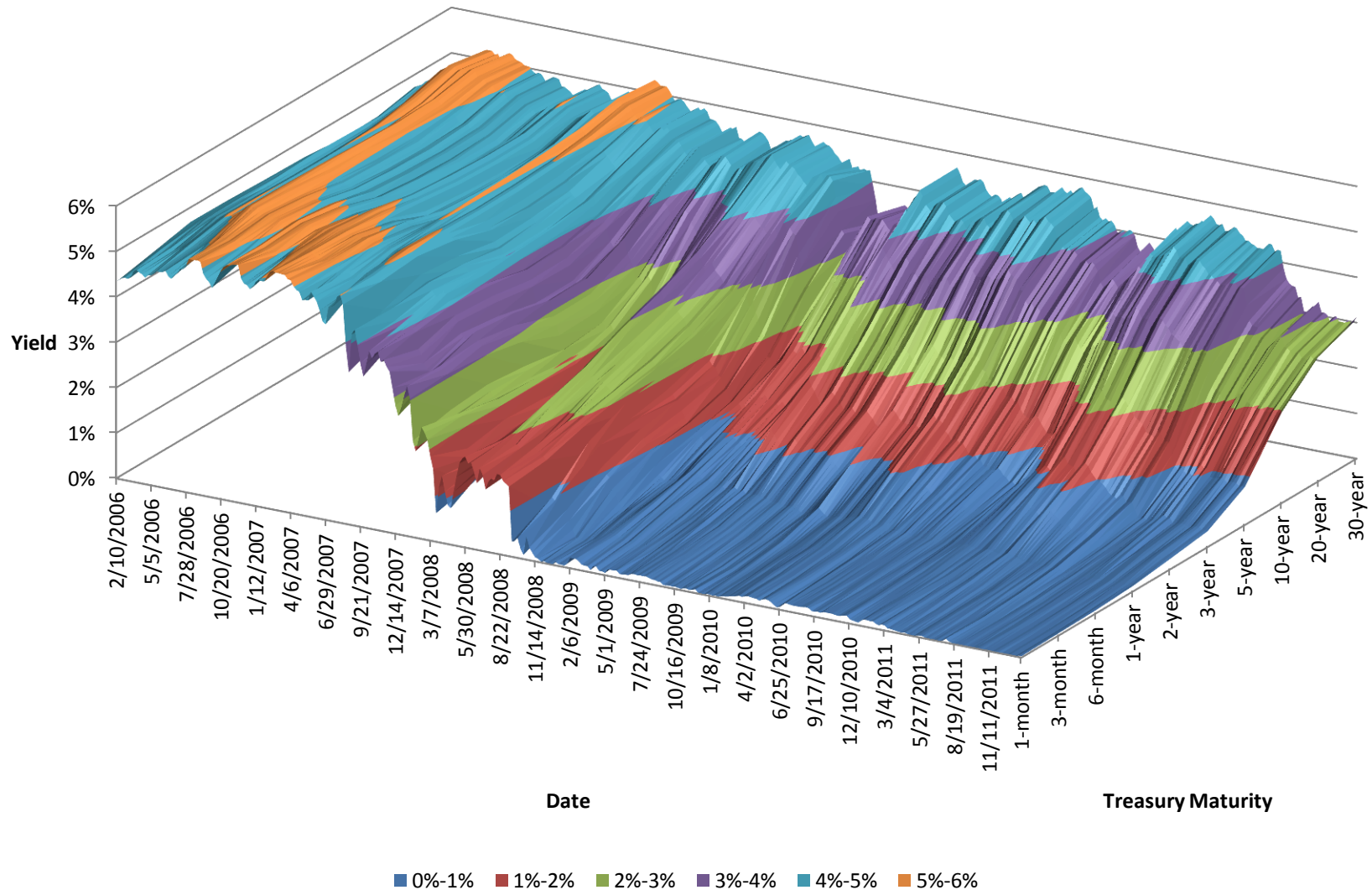
Most Federal Open Market Committee (FOMC) participants believe the first, appropriate increase in the Target Fed Funds Rate is 2014 or later.

Number of FOMC Participants



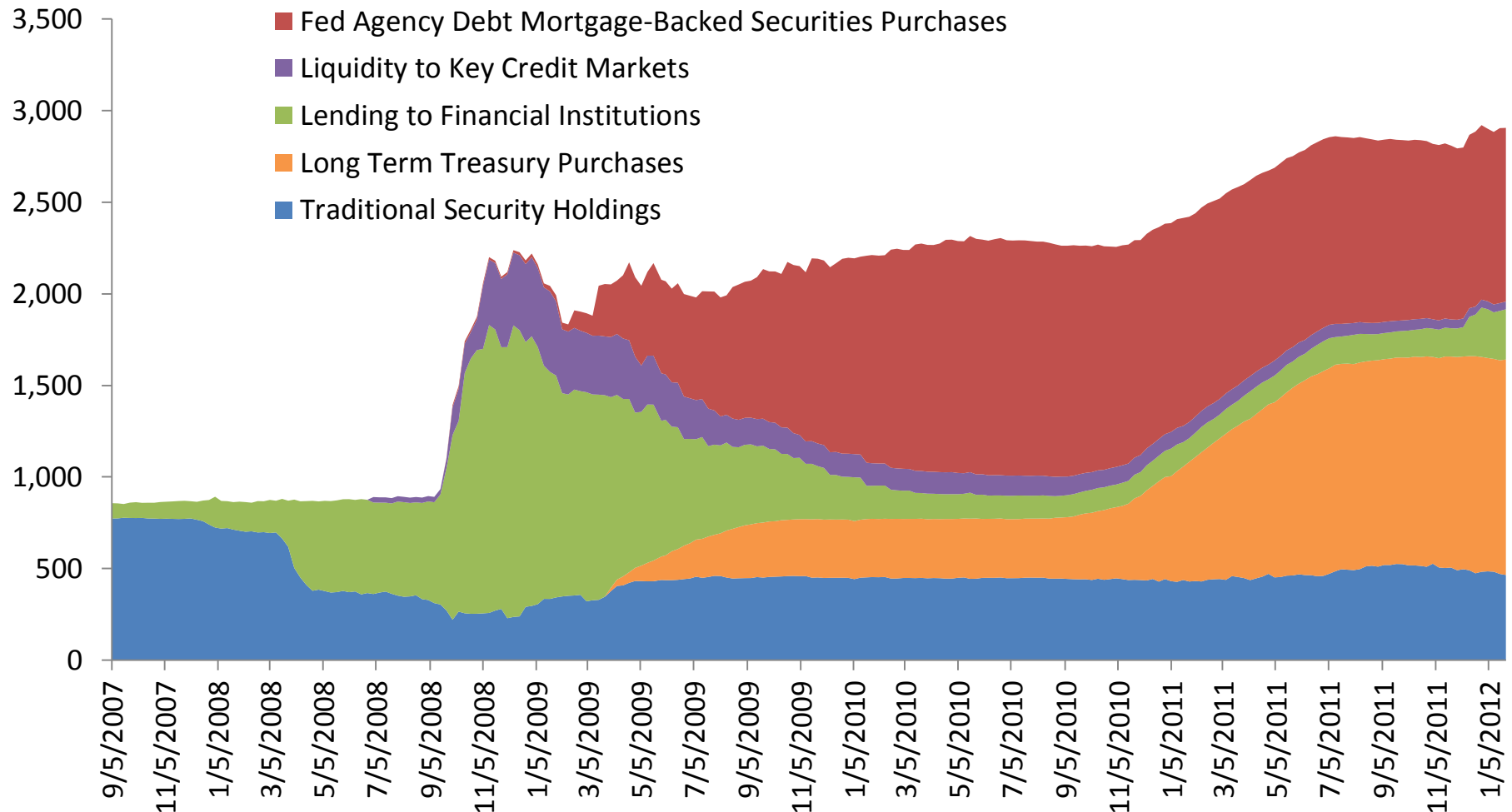
Source: Federal Reserve Board of Governors (The number of FOMC participants who judge that, under appropriate monetary policy And in the absence of further shocks to the economy, the first increase in the target federal funds rate from its current range of 0 to ¼ Percent will occur in the specified calendar year.

Could longer term interest rates creep up in mid-2012 or will there be QE3?



How does the Fed return to a more “normal” balance sheet?

Billion Dollars



Source: Federal Reserve Bank of Cleveland

Concluding thoughts.

- Today, most farmland values can be justified given current market conditions.
- Yet, plenty of risks and questions surround the sustainability of farmland values.
 - Rising interest rates would likely put downward pressure on land values.

Concluding thoughts.

- John Blanchfield, who runs the ABA Center for Agricultural & Rural Banking at the American Bankers Assn. stated, “The FDIC is convinced there’s a (farmland value) bubble, and they’re not going to miss this bubble, by God.”
 - <http://www.businessweek.com/magazine/farmland-is-pricey-the-fed-is-worried-10132011.html>
- In the end, we have to ask ourselves if talking about a land value bubble is the right risk to focus our attention on.

Thank you.

Questions?

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