



If you've been following reporting on farmland prices, you might be under the impression that the agricultural land market, where values have more than doubled in Farm Belt states like Iowa and Nebraska from 2009 into 2013, is about to experience a bust not unlike what the housing market faced in 2008. But despite isolated reporting on declining values and alarmist predictions that try to draw parallels to the farm crisis of the 1980s, many agricultural economists say the picture isn't even close to bleak.

"This has been a remarkable market to watch," says Bruce Sherrick, Ph.D., director of TIAA-CREF Center for Farmland Research at the University of Illinois. "People keep saying farmland prices can't continue to go up, but they are."

And that is despite falling commodity prices. In 2012, in the wake of severe drought conditions around the country, corn was selling at more than \$7/bushel while today's prices have dropped by more than half to \$3.25. And corn future prices at the Chicago Board of Trade have dropped 24 percent in the last year. The Federal Reserve reported slight declines in land prices in the St. Louis, Kansas City and Chicago districts in the first

quarter of 2014, but observers on the ground say, overall, land prices continue to climb, if less dramatically, in most places. "A lot of the commentary has come about from observing patterns that look unsustainable," Sherrick notes. "Farmland, at its core, is a capitalized set of future income expectations."

But even if land prices should decline in the coming months and years (and plenty of economists and appraisers don't think that will happen), Sherrick says today's producers are not holding highly leveraged assets the way they were in the 1980s. "Back then, we had interest rates on loans of 17 to 20 percent and loan-to-value ratios of 15 percent," he says. Now, he points out, average loan-to-value

ratios are around 50 percent. "In the 80s, you needed 12 percent just to service your interest. Now you need only 2 1/2 percent."

Not only do today's producers have more equity (thanks to growing incomes over the last few years), but they also have much better financial protection in the form of crop insurance, which was virtually nonexistent in the 80s. "We may see some softening in the land market," Sherrick says, "but nothing major."

Not all economists agree. Some think that farmers' reduced revenues will eventually cause as much as a 20 to 25 percent correction in land prices in the coming years. In February, the U.S. Department of Agriculture

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predicted that farmers’ net income will drop by 27 percent this year to \$98.5 billion, the lowest since 2010.

Marcia Zarley Taylor, executive editor of DTN/The Progressive Farmer, says land values tend to mirror farm income, but even if commodity prices stay low for several years, that won’t correspond to an immediate reduction in land values. In a June 5 blog post, Taylor wrote, “There’s always a lag though, as in the 1980s when farm incomes fell first, but the price of land didn’t bottom for five or six years.”

However, even with reduced incomes compared to 2012, the nation’s producers will be okay, both because they are not

carrying highly leveraged debt and because crop insurance “places a floor under losses,” as Sherrick says. “You have to remember that commodity prices don’t have a lot to do with income.”

Plus, a lot of producers have turned fields from corn to soybeans. “Soybean markets are holding up quite well,” says Larry Janssen, professor of agricultural economics at South Dakota State University. Cattle prices are holding strong as well, which is keeping range-land prices up.

Janssen says the majority of ag-land sales are to producers who are expanding operations and who have plenty of cash to work with, meaning their down payments on loans

are fairly substantial. “One of the signals I look for is cash rental rates,” he explains. “If they’re still moving in the same direction as prices, that’s a proxy for returns on land.” In South Dakota, for example, 4 out of 10 acres are rented on cash or shares.

Appraisers on the Ground See Continued Blue Skies

Robert Grace, MAI, SRA, of Grace and Sons Appraisal Service in Shawnee, Oklahoma, says he’s seeing prices going nowhere but up in his region. “We’ve had steady 5 percent year-over-year increases, and I think it will continue that way,” he remarks. “Land here is affordable, and it’s seen as a safe investment.”

Grace says prices in Oklahoma right now range from \$1,000/acre up to \$6,000/acre. "I think it will eventually level off," he says. "Prices have peaked because land has been so undervalued for so long." He anticipates more moderate price increases in the future, probably around 3 percent per year.

One of the things driving up land prices is supply and demand. He says producers, once they have land, tend to hold onto it. "There is not a lot of supply, which is contributing to rising prices," Grace adds. He says cash rents in Oklahoma continue to go up as well, ranging from \$15 to \$80/acre depending on land quality. And he doesn't see softening commodity prices driving land prices down. "Most of today's buyers are driven by the long-term view," he says. And they also have more cash on hand to buy these days, in part because of the oil and gas boom in Oklahoma and Texas, which has increased the overall wealth of the population.

Who's buying all this land? It's not institutional investors, as one might presume. According to Sherrick, institutional investment in agricultural land accounts for 0.4 percent of a \$3 trillion asset market. The vast majority of the buyers are producers looking to expand their operations, buy contiguous parcels or purchase family land.

Brian Gatzke, Candidate for Designation, owner of Northern Plains Appraisal, LLC, in Brookings, South Dakota, says producers will actually pay more for land than investors, and farmers are now enjoying financing opportunities from private equity groups like Rabo AgriFinance, based out of the Netherlands. "Within five

years, they've become a major force in big ag-land financing," he remarks, noting that they are competing hard with Farm Credit financing.

Gatzke says there are actual land shortages in his state. "Some livestock producers are going to dry lots because of the shortage of grassland," he remarks. Many farmers converted to row crop production when corn, soybean and wheat prices started soaring,

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reducing the state's grazing land substantially.

Gatzke says prices in South Dakota are coming in at around \$2,000/acre for pasture and \$8,000 to \$10,000/acre for cropland. However, he's seen prices occasionally jump even higher. "In June, there was an auction for 80 acres, and it sold for \$13,800/acre," he remarks. "That's high even for good quality cropland."

The rapid pace of rising values has slowed in the last year, however. According to the 2014 South Dakota State University South Dakota Farm Real Estate Survey, average land prices in South Dakota increased 6.1 percent from 1991 to 2014, compared to 16.5 to 33.6 percent increases in the previous three years. Across the board, South Dakota land prices have more than doubled since 2010 and increased sevenfold since 2000.

However, Gatzke thinks prices are at the top of the curve in most regions, though he's seen 10 percent increases in values in the eastern part of South Dakota in the last year. "If corn prices go below breakeven, that will have an impact," he explains. "Farmers may elect to keep their grain in storage for one to two years until commodity prices return."

He thinks rent prices are capped out, however, as he's seeing high-productivity land renting for as much as \$400/acre. "That's high," Gatzke says, "and not sustainable."

Michael Burger, MAI, owner of Michael Burger & Associates in Bakersfield, California, says "current prices are at the highest they have ever been." Part of the land price increases in California is due to increased profitability resulting from permanent plantings like almonds, walnuts, pistachios and

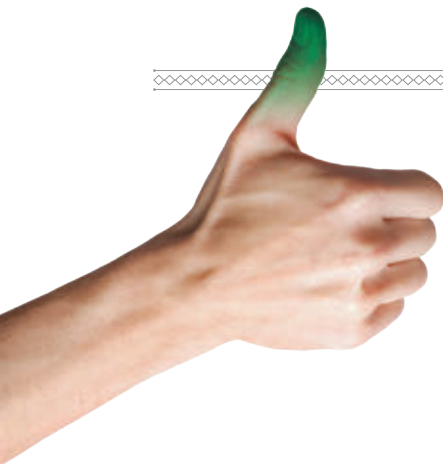
All Thumbs

The balance sheet for agricultural land looks healthy, according to data from the Economic Research Center at the U.S. Department of Agriculture:

Farm real estate assets total more than \$2.9 billion.

Farmland represents 82 percent of total farm assets.

Farm real estate debt is only 59 percent of total farm debt.



grapes. “The increased profits in these crops are driving the open-land prices up as more permanent planting growers compete for open land,” Burger explains.

In the West, however, water always is a concern, and Burger says if drought conditions continue, it will drive values for property with water even higher. “Water quality and quantity is a primary factor affecting land values.”

Burger adds that low interest rates, declining or volatile investment returns in other markets, demand overseas and increasing producer incomes due to new technologies, new plant varieties and the resultant increases in yields are all combining to drive prices higher in some regions.

In the San Joaquin Valley, where Burger performs most of his valuation work, irrigated farm land is selling for \$15,000 to \$20,000/acre whereas as recently as 2010, prices for land with water stood at around \$10,000/acre. In areas impacted by drought where there is no guarantee of year-round water, sale prices are running \$8,000 to \$14,000 per acre. Meanwhile, the rents for Valley land with water are reaching \$300/acre when a year earlier they were \$150. Burger says he recently saw one tract go for \$20,000/acre. In California at least, those prices are in line with commodity prices, and Burger doesn’t think a correction is likely, at least not in the next 12 months.

Sherrick says when one sees sales like that, however, it’s typically a producer buying a neighboring piece of property.

Carl Stillman, MAI, president of Stillman and Associates in Salem, Oregon, sees much more variation in the land market in the Willamette Valley. “In this area, we have a lot of micro-markets,” he says. “Good quality irrigated land is increasing in value and has

been for a number of years.” He says the land market is still not back to pre-2008 prices, however. He expects prices in his region to keep rising.

Right now, the market ranges from \$3,500/acre for lower-quality, non-irrigated land to \$5,500/acre for top-quality, irrigated property. Stillman says he is starting to see more activity from investors who want to place capital in agricultural land. “Farmland doesn’t typically give a high rate of return,” he says, “but investors are looking to get 6 percent.” Janssen agrees with this, noting that some investors feel safer buying land than putting money in the stock market right now.

The highest earning crops right now in the Willamette Valley are blueberries and hazelnuts. “Most of the commodities out here are doing very well except grass seed varieties,” Stillman says. “The nursery industry is still suffering a lot.”

He does think prices will start leveling off in the not-too-distant future, however. “Farming is a boom-and-bust business and always has been,” he notes. “Now is a good time to be in agriculture.”

Stillman says anyone who thinks there is going to be a massive collapse in land values is behind the curve. “Farmland disappears at a pretty good clip,” he remarks. “The need for food and fiber continues to grow.”

Appraising in a Volatile Market

How do you appraise land in such a volatile market? Grace says it’s tricky, particularly in a market like his where land transactions are few. He says he looks at older sales and applies 5 percent to account for current market conditions, and he also looks at sales outside a particular tract’s locality that have “like” characteristics.

Gatzke says farmers have experienced major gross income changes the last few years, which has helped escalate land prices by as much as 20 to 30 percent per year in some areas, though he thinks those increases are now leveling out in South Dakota at about 10 percent. “What is the true market value of a piece of land now?” he asks. It’s hard to say with so much volatility still in the market.

“Appraisal is normally based on sales analysis,” Gatzke says, but with land prices rising so quickly it’s a challenge to value land.

“It’s a difficult market for appraising land values right now,” Sherrick says. “Only about 1 percent of farmland overturns per year.” That means the comparables just aren’t out there. So appraisers look at drainage, irrigation, buildings and proximity to markets. “People look at extreme sales and think that’s what farmland is worth,” he adds, “but the middle 50 percent of sales is pretty reliable. You add to that the value of any extreme characteristics.”

“People buy land not only for access to producing from it, but out of a strong expectation that over time land will appreciate,” Janssen says. He says he doesn’t expect prices to go down in the near future, though it could happen several years out. “There’s a good chance of modest declines because corn, wheat and soybeans aren’t going to stay at these prices forever,” he adds. “The offset of that, however, are strengthening export markets.”

Sherrick says that even if there was an overall 20 percent dip in land values (which he does not anticipate), it wouldn’t cause much of a ripple. “Farmers have a lot more equity now,” he explains. “It will change wealth, but it won’t trigger a sell-off.”

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According to the TIAA-CREF Center for Farmland Research, there are five big risks to agriculture land values:

A significant change in water availability and usage.

A sudden reversal of monetary policy.

Significant changes in future crop insurance provisions.

A global slowdown in income growth.

A major change in renewable fuel standards and related policies.