FARMLAND PRICES: CAN WE AFFORD TO OWN THE LAND WE FARM?
Sometimes it seems pretty clear to us that the “wheels are coming off”.

So we might ask..... Are high farmland prices heading us for a big wreck?
But your perspective can change once you see the big picture!

Sometimes things just balance out.
Farmland Prices: Can we afford to own the land we farm?

What I’ll Cover:

1. Background on my perspective
2. What about these land prices?
3. What is affordable?
• Business opportunity to work with land investors and growing farmers
• Based on ag expertise; focus on sustainability
• Client Services
  • Land management & JV farm management
  • Due diligence
• Farmer partners
  • Cash & flex rental and JV agreements
Farmland Prices
The Farmland Market

Keep in mind:

• Farmland is a commodity market: there are bulls and bears

• “Markets are weird: Every time one person sells, another one buys, and they both think they're smart!”

• Land often has non-business sentiment attached plus the overlay of market emotions: fear & greed
Globally Land Values Are Rising

Key factors:

• Growing World Population
• Increasing Standard of Living
• Supply of Arable Land and Water
• Food Security Concerns
• Food Crisis (perception or reality)
• Bio-fuels
More Key Factors

• Political Instability
• Environmental Sustainability/Global Warming
• Technology Issues (GMO)
• Social Trends (Organic, 100 mile diet)
• Food Safety Issues (Traceability)
• Mega farms in Eastern Europe and SA
• Fear of Inflation and/or Collapse of the Fiat Money System
Globally

As a result, globally “agriculture” and arable farmland is a **HOT** investment segment. This includes land and farms in Western Canada.

But....we have land ownership restriction

It’s a matter of perspective:

“The more time I spend here the more expensive our land seems. The more time I spend in other places of the world the cheaper it seems here.”
Canadian Prairies Agriculture

The global and economic factors draw outside attention to Western Canada (Sask).

What do they see?

• Relatively cheap land (ROI)
• Fragmented land ownership
• Good farmers: production ability, adoption of technology and land stewardship
• Good infrastructure
• Political stability
Local Perspective

Why is the price of Sask farmland rising?

• Our grain economy is strong: crop prices and interest rates.

• Farmer equity is rising.

• A business imperative to grow farm unit size: rising costs and economies of scale.

• More non-farmer and non-local buyers in the market.
Who is driving the price up?

OR

Local farmers?  Outside buyers?

Both?
Who are these outside buyers?
A wide range of buyers from different backgrounds and geographies with various goals, objectives and motivations.

- Investment “funds”
- Individual investors
- Immigrant farmers
- Corporate farms and geographically dispersed family farms

Having these buyers in the market does not mean the price will continue to increase.
Predicting Future Land Prices

One thing I have learned……..

What goes up eventually comes down and….

What comes down eventually goes up!

My guess is…..
This Price Run-up Will Not Continue

Not in a bubble but a “correction” will occur.

A leveling off or more likely a short term drop.

Longer term my outlook is bullish.

More buyers means a deeper land market
BUT
they can be and are significant sellers too!
What could trigger a correction?

- Weakening of margins for crops
  - Price drop due to increase in production globally
  - Increase in input costs
- Rise in interest rates
- Discouraging production year(s)
- Demographics: the “baby boomer” bulge in farmer population
  - At some point fear will kick in and increase the supply
Can we afford to own the land we farm?
Land Price vs Productive Value

“Land prices are just too high - it just can’t pay for itself”

YES.... but it’s always been that way!

And that has never stopped farmers from buying it.

Let’s be clear - the question is about affordability not price vs productive value.

Affordability is determined farm by farm.
Affordability

Consider the varying points of view of farmers:

• Retiring farmer with no successor
• Retiring farmer with a successor
• Late career farmer (High equity/no debt)
• Mid career farmer (Some equity/some debt)
• Beginning farmer (low equity/few assets or a lot of debt)

A matter of circumstance and timing………some can afford to buy land - some can’t; and some don’t care and are pretty happy with high prices!
Has it ever been less affordable?

Central Alberta Example

<table>
<thead>
<tr>
<th></th>
<th>1981</th>
<th>1993</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land Value</td>
<td>$1,200</td>
<td>$800</td>
<td>$3,000</td>
</tr>
<tr>
<td>Interest Rates</td>
<td>15%</td>
<td>10%</td>
<td>5%</td>
</tr>
<tr>
<td>Annual Payment (20 year term)</td>
<td>$190</td>
<td>$94</td>
<td>$240</td>
</tr>
<tr>
<td>Gross Revenue</td>
<td>$159</td>
<td>$185</td>
<td>$386</td>
</tr>
<tr>
<td>% Revenue to Pymt</td>
<td>120%</td>
<td>51%</td>
<td>62%</td>
</tr>
</tbody>
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Courtesy: Merle Good, Tax Specialist, AARD
Op Co and Land Co

Farm management trend is to separate the farm business (Op Co) from land ownership (Land Co or personal).

Now think about the land you own as an investment.

What does the land purchase decision look like now?

Would or can you buy more?

The million dollar question.
# Affordability

## Central Alberta Example

<table>
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<th>Per Acre</th>
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<td>(20 year term)</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Market Cash Rent</td>
<td>$40</td>
<td>$45</td>
<td>$80</td>
</tr>
<tr>
<td>Paymt to Rent Ratio</td>
<td>4.75</td>
<td>2.08</td>
<td>3.0</td>
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*Courtesy: Merle Good, Tax Specialist, AARD*
Affordability

Combining the Op Co/Land Co thinking with your ratio of payments to rent gives a new perspective and a different way to approach budgeting a land purchase.

If you have debt free acres, can your Op Co afford to pay your Land Co fair market rent on those acres so it can make the payments on additional new acres?

In our example, the ratio would be market rent on 3 quarters to purchase 1 new quarter.
Assets = Liabilities + Equity

“I can get the mortgage – it must be okay”

Be careful with debt: in an over heated perhaps inflated land market you need more margin of safety in repayment ability and strong D/E.

The lender is managing its downside risk (not yours) by the loan to value – that is, your equity in the deal.

How are you managing your downside risk?
Leverage

Lenders base their LTV on current market value. That’s good news in a rising market as the value of all your land goes up and so does your ability to leverage.

But it’s bad news in a falling market as your leverage % goes up even on existing debt and mortgages can go under water.

Some of our investor clients use leverage – most stick to 50% or less.
So what’s a young guy do?

Every situation is different in terms of how much family support is available.

Buy some land, with a safe level of debt, to build equity.

Rent land and look for other opportunities to use outside equity to gain scale and grow profit.
Outside Equity

Can serve several purposes:

1. Enable growth.
2. Increase the speed of growth (sweet spots).
3. Share ownership and production risk. (Equity is risk capital – Debt is not)
4. Enable succession/equity take-out of partners.

Many other sectors use outside equity for growth – production agriculture can do the same.

We have seen several good success stories.
Some Options for Outside Equity

- Renting land
- Machinery Leasing
  - The residual value is someone else’s equity
- Direct investment
  - \( A = L + E \)
- Joint Ventures
  - Production JV
  - Whole farm JV
What are investors looking for?

- Competitive rate of return
- Return from rent, risk and capital appreciation
- Investment portfolio diversification
- An inflation hedge

“Gold with a dividend”

Some are also interested in:

- Green – environmental sustainability
- Food safety, organic and/or food security
- Flipping
Ideal Investor for Sustainability

• Long investment timeframe
• Reasonable annual return expectations
• Prepared to share risk through flexible cash rent or joint ventures to increase returns (risk/reward)
• Understands the variability of production agriculture
• Recognizes and values agriculture industry knowledge
Take Aways

• Think about the land market like any other market. Watch for a correction in the price.

• Farmland investors are a force in today’s farmland market - learn about them and use them to further your business goals.

• Farmland has been a good investment for farmers and others so buy what you can afford as an investment but don’t put your business at high risk with excessive debt - there are other ways and sources of equity to grow your farm!
Thanks!