

# Farmland

## IN PERSPECTIVE

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*Goodwin & Associates Real Estate, L.L.C.*



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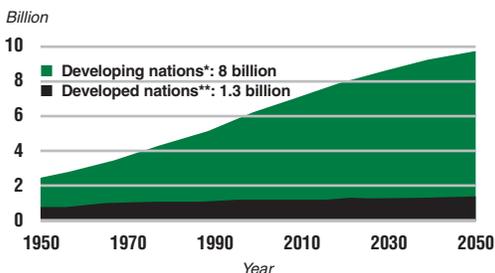
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### World population reaches 7 billion milestone

The world's population has reached 7 billion and is projected to reach 10.1 billion in the next 90 years, according to a recent United Nations world population report "The World at Seven Billion and threats to the world's supplies of food and water are looming."

At current fertility rates, high-fertility countries are expected to triple their medium-variant populations to 4.2 billion by 2100, according to the report. The population of intermediate-fertility countries, accounting for 40% of the world's people, would increase by 26% to 3.5 billion, while that of low-fertility countries — such as China, Brazil, Indonesia, and most countries in Europe — would decline by about 20% to 2.4 billion.

#### Bulk of population growth seen in developing countries



\* All countries in Africa, Asia (except Japan), Latin America and the Caribbean, and Oceania (except Australia and New Zealand)

\*\* All countries in Europe and North America, as well as Japan, Australia and New Zealand

### LEASING TRENDS

## What should my farm earn?

By Gary Schnitkey

Increases in commodity prices in 2011, combined with price volatility, make it difficult to say what each farm should earn in the current agricultural environment. One thing is certain though: returns to farmland have been increasing in recent years.

Average cash rents over time illustrate increasing returns. In Illinois, for example, average cash rents in the state from 2005 through 2010 have increased by 41%. Similar increases have been seen over many Midwest states: 39% in Indiana, 50% in Iowa, 45% in Michigan, 56% in Minnesota, 55% in Nebraska, 34% in Ohio, and 41% in Wisconsin.

These increases illustrate general trends, but don't show the overall variability that exists in cash rents. Rents vary tremendously among farms. For example, USDA reports that average cash rent by county in 2010 varied from \$74 per acre to \$260 per acre. For example, the county with an average cash rent of \$260 per acre could have rents plus or minus \$130. Many factors impact this variability. In answering the question "What should my farm earn?" seven principles are important.

**Knowledge is power:** Knowledge is necessary to obtain the proper earnings for a farm. Not having knowledge about the farm and the current economic environment places the landowners' ability to obtain competitive returns at the mercy of the individuals renting the farmland. Gaining knowledge requires time and effort. Among the best assets landowners have in gaining this knowledge are professional farm managers, farmland Realtors, land grant university extension offices, and area farmers.

**Know your risk tolerances:** Landowners who bear more risk generally get higher returns to their farmland. In this environment, many professional farm managers are moving to variable cash rent arrangements, which vary the rent depending on actual yield and prices. With a variable rent arrangement, the landowner does not know the actual rent until prices and yields are determined in the fall. But the landowner has the potential to share in higher returns resulting from high commodity prices and high yields.

Continued on page 2

Similarly, many cash rents now are being set at what may seem to be high levels. Given the current price environment, high cash rent levels are supported. In future years, however, these rent levels will come down if commodity prices fall. Individuals who take a lower rent when commodity prices fall can obtain higher cash rents now.

**Know the productivity of the farm:** The productivity of the farmland has a large impact on its returns. For example, a farm that can reasonably expect to average 200 bushels per acre of corn will get a much higher return than a farm that averages 150 bushels per acre. Knowing the soils on the farm, conditions of farmland improvements, and previous yields from the farm will aid in understanding the productivity of the soil.

**Know what is happening to commodity prices:** Commodity prices drive farmland returns. Between 1975 and 2006, corn prices in the United States averaged about \$2.40 per bushel. Since 2006, prices have been much higher (see *Figure 1*), leading to higher farmland returns. Also since 2006, prices have been much more variable leading to

more difficulty in determining cash rents. It is not unusual to see \$.50 swings in corn prices within a few days. A \$.50 decrease in corn price on farmland that produces 180 bushels per acre leads to a change in revenue of \$90 per acre (\$.50 per bushel x 180 bushels). This change in revenue then impacts the return a landowner can receive for farmland.

During 2011, commodity prices were high. In August 2011, corn prices averaged \$6.88 per bushel across the United States (see *Figure 1*), the highest average price ever. Pricing backed off some in September – the price averaged \$6.69 in September, down \$.19 from August levels – commodity prices were at high levels in late summer and early fall when many cash rents were being determined for the coming year.

**Know what is happening to costs:** The non-land costs of producing crops have been increasing. In corn, for example, non-land costs have increased from \$250 per acre in 2000 to an estimated \$500+ per acre in 2012 (see *figure 2*).

Higher costs have two impacts. First, they decrease the amount the

farmland earns, lowering cash rents. Without increases in commodity prices and yields, the increases in non-land costs would have caused decreasing returns to landowners since 2000. Second, higher costs increase risks. Much higher commodity prices are needed to have profits within agriculture. Reductions in commodity prices could lead to downward pressure being placed on the returns landowners receive.

Knowledge is key to getting the return that farmland should earn. Overall, the outlook for 2012 is bright if commodity prices remain at high levels. In going forward, an understanding of the economic situation as well as an understanding of the lands' earning potential will aid landowners.

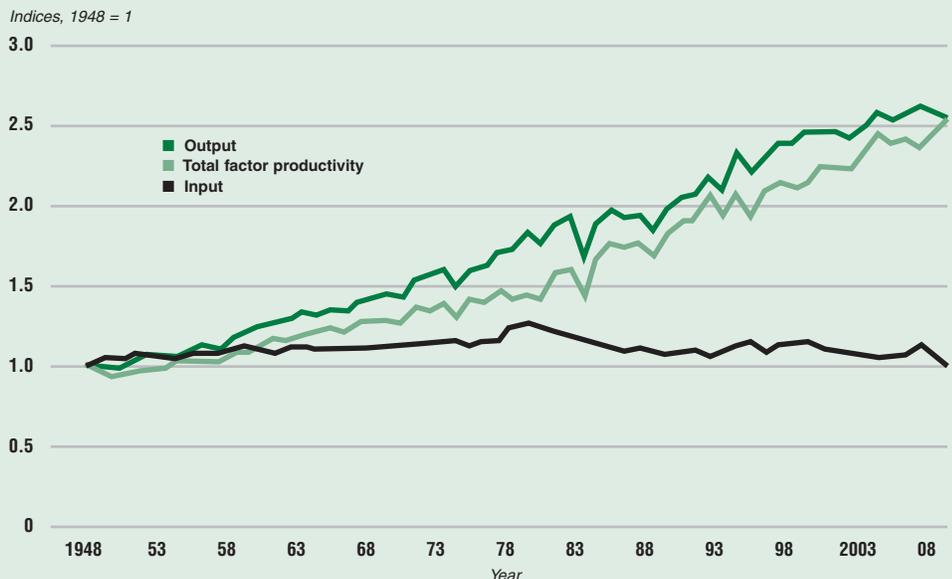
**Dr. Gary Schnitkey** serves as a professor and farm management specialist in the Department of Agricultural Economics, University of Illinois. His extension activities focus on risk management and farm income evaluation.



## U.S. agricultural productivity continues to rise

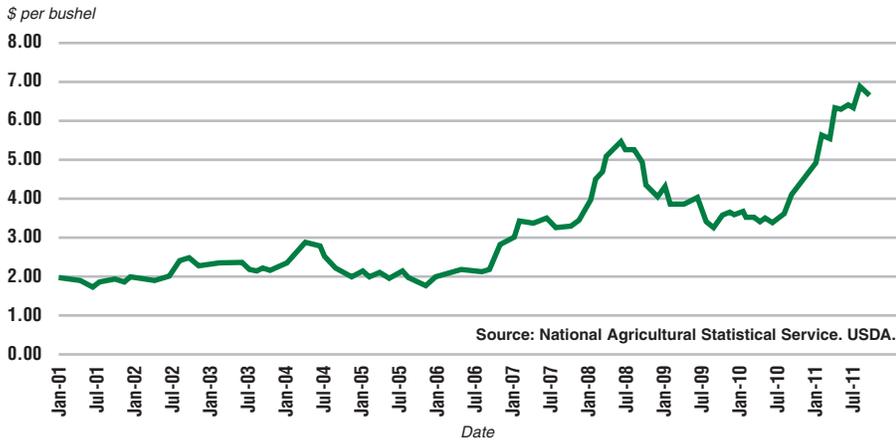
Data from the Economic Research Service (ERS) shows that total farm output grew by 158% in the 60 years from 1948 to 2008, but total inputs used in agriculture remained largely unchanged. However, the composition of the input mix changed dramatically. While labor use declined by 78% and land use by 28% during those years, chemical use grew fivefold from 1948 to 1980 before leveling off. Nevertheless, total factor productivity growth in U.S. agriculture over the period has been steady, at 1.52% per year, a rate exceeding that of a majority of other U.S. industries and of most other nations' agricultural sectors.

### U.S. agricultural input use was steady while total factor productivity expanded from 1948 to 2008

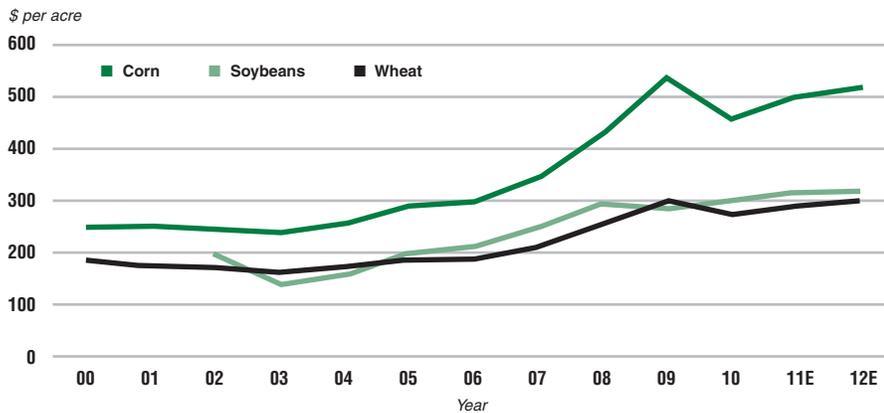


Source: USDA, Economic Research Service, Agricultural Productivity in the United States, [www.ers.usda.gov/data/agproductivity/](http://www.ers.usda.gov/data/agproductivity/)

**Figure 1. U.S. monthly corn prices, January 2001 to September 2011**



**Figure 2. Non-land costs of producing corn, soybeans and wheat, 2000 – 2012**



## Stocks-to-use totals near record low

The ratio of global ending stocks to total use can be a reliable indicator of market prices: the lower the ratio, the tighter the market and the higher the price. The stocks-to-use ratios for corn and soybeans approached record lows during 2011. The stocks-to-use ratios for wheat and rice suggested reasonably comfortable stock levels.

$$\text{Stocks to use ratio} = \frac{\text{Inventory remaining from the previous year} + \text{the current year's total production} - \text{total amount used}}{\text{Total amount used}}$$

## Stocks-to-use ratio for total world grains and oilseeds near record low in 2011



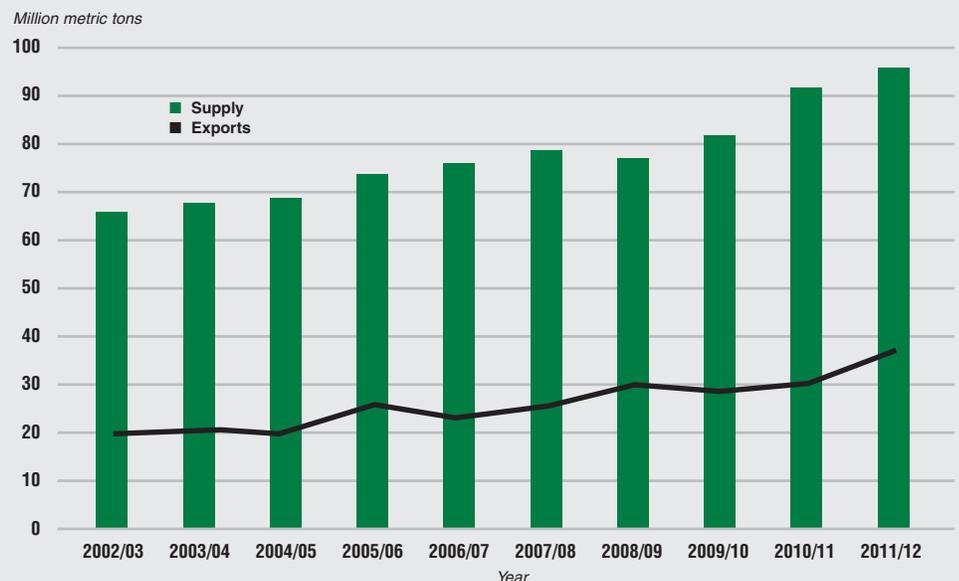
Note: Oilseeds include annual crops of soybeans, rapeseed and sunflowers.

Source: USDA, Economic Research Service using USDA's World Agricultural Supply and Demand Estimates and Production, Supply and Distribution database, February 2011.

## Brazil sees record soybean supply

Brazil produced a record 2010/11 soybean crop, estimated at 75.5 million tons. The projected soybean area for Brazil in 2011/12 remains unchanged at 25 million hectares, up 3% from 2010/11. Corn will continue to compete strongly for cropland.

## A record soybean supply in Brazil is seen to expand exports



Source: Production, supply and distribution database. Foreign Agricultural Service. U.S. Department of Agriculture. August 12, 2011.

# Farmland IN PERSPECTIVE

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