Farmland IN PERSPECTIVE

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GOODWIN

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How Dependent are Ag Industries on Overseas Markets?

U.S. agriculture is twice as reliant on overseas markets as the general economy, according to the Economic Research Service of the U.S. Department of Agriculture (USDA). Agriculture's export reliance, measured as exports divided by farm cash receipts, ranged from 26% to 30% during the mid-1990s.

Bulk commodities have long depended on overseas markets. Nearly half of the U.S. wheat and rice crops are exported; about one-third of its soybean, tobacco and cotton production is shipped overseas; and 20 percent of the corn crop is exported. High-value products, including fruits, vegetables and animal products, are increasingly dependent on overseas markets as well, and many are approaching or have already reached the same level of export dependency.

Suppliers of high-value products have seen export sales outpace domestic sales by a wide margin since the mid-1980s. Today, for example, nearly 60% of U.S. cattle hides are exported, with a total export sales value of $1.6 billion. The export dependency of the almond industry is even higher, with 67% of the crop shipped overseas. One third or more of fresh table grapes, dried plums, raisins, canned sweet corn, walnuts and animal fats is exported.

The Financial Power of Investing in Land

By Chris Hurt • Agricultural Economist • Purdue University

The attorney's call got me to thinking. In 1999, he represented a family with Midwestern farmland that was held in a trust. The trust had been established by their grandfather in his estate. Ironically, Grandpa had died in the 1960s. His trust specified that the farm could not be sold until at least the year 2030, as he believed that over time farmland would be a favorable investment for future generations.

The heirs were not "money hungry." They simply felt Grandpa was not right to tie up capital in farmland for such a long period. They wanted to maintain the trust, but sell the land and reinvest the money in the stock market where returns were so much higher.

Indeed, those were days of lofty returns on Wall Street. For the five years from 1995 to 1999, the annual rate of return for the S&P 500 plus dividend yield averaged 28 percent. Stocks versus dirt seemed a "no brainer" at the time.

The issue had to go before a judge. The family's argument was that Grandpa had simply made a mistake by tying up money for way too long in a poor-performing asset. They further argued that Grandpa's primary objective was to provide financial assistance for future generations of his family, and thus selling the land now and converting the proceeds to stock would better achieve Grandpa's goals.

Was Grandpa correct to tie up money in farmland for so long?

Farmland vs. Stock

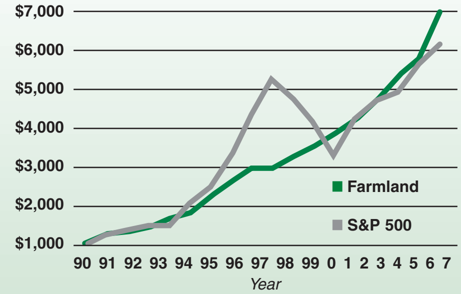
Let's look at the more recent past for some clues. It is hard to imagine that almost any major form of investment could have done as well as the stock market in the last-half of the 1990s.

So let's compare returns for farmland to stocks starting in 1990.

Returns for the Standard and Poor's 500 stock index, commonly known as the S&P 500, will be used. The annual percentage returns are based on two factors. First, the appreciation in value of the stocks as measured by the percentage change in the S&P 500 index each year, and secondly the average yearly dividend yield.

Continued on page 2

Value of $1,000 Investment in 1990 (Pre-Tax): Indiana Farmland vs. S&P 500



Financial Power *cont. from page 1*

Land has a similar two-component measure: the annual change in the value of land and the adjusted cash rent. For the comparison, land values from the Purdue Land Values Survey from a mid-year survey will be used. While the data is from Indiana, it should be broadly reflective of most Midwestern farmland. The annual cash rents are reduced by property taxes, the cost of applying lime, and a moderate management fee.

In the 18 years from 1990 to 2007, the stock market as measured by the S&P 500 has been an adventure ride with annual average returns of 11.74 percent, but with average variability near 17 percent (measured by the standard deviation of returns).

Overall returns for farmland are similar with an annual average of 11.54 percent. But, farmland owners only had about a five percent average variability, and thus a much calmer ride when compared to stock investors.

The stock investors had bragging rights for their great returns in the stock market in the last-half of the 1990s, but who has the bragging rights today? For an answer, the value of $1,000 invested in the stock market (S&P 500 returns) in 1990 is compared to the same $1,000 invested in farmland (assuming all returns are reinvested and on a pre-tax basis). It is true that by New Year's Day of 2000, the stock investors were flying high. Their $1,000 investment had grown to about $5,200, and the farmland investor's value, while still very respectable, was only worth $2,900.

But today, those bragging rights go to the holders of farmland. The stock market had a downward correction in 2000, 2001, and 2002, falling by 37 percent. Meanwhile farmland continued its march higher. Today, that $1,000 invested in farmland in 1990 is worth about $7,000. Investments in stocks have recovered, but trail with a value of about $6,000.

Back to Grandpa

Now back to the attorney's question. Was Grandpa correct in tying the family's wealth to farmland for so long? Grandpa was <u>not</u> unreasonable. My study, and others, have indicated that over the long run, farmland has achieved returns that are nearly equal with the stock market, but with much less year-to-year variability. Both the stock market and farmland are subject to wide swings, but those wide swings have been much more frequent in stocks.

When looking at investment returns over just a few years, timing is everything. Great timing makes investors look like wizards and poor timing like dunces. Thus making decisions to shift large investments from one investment type to another should be made with a view to the long run.

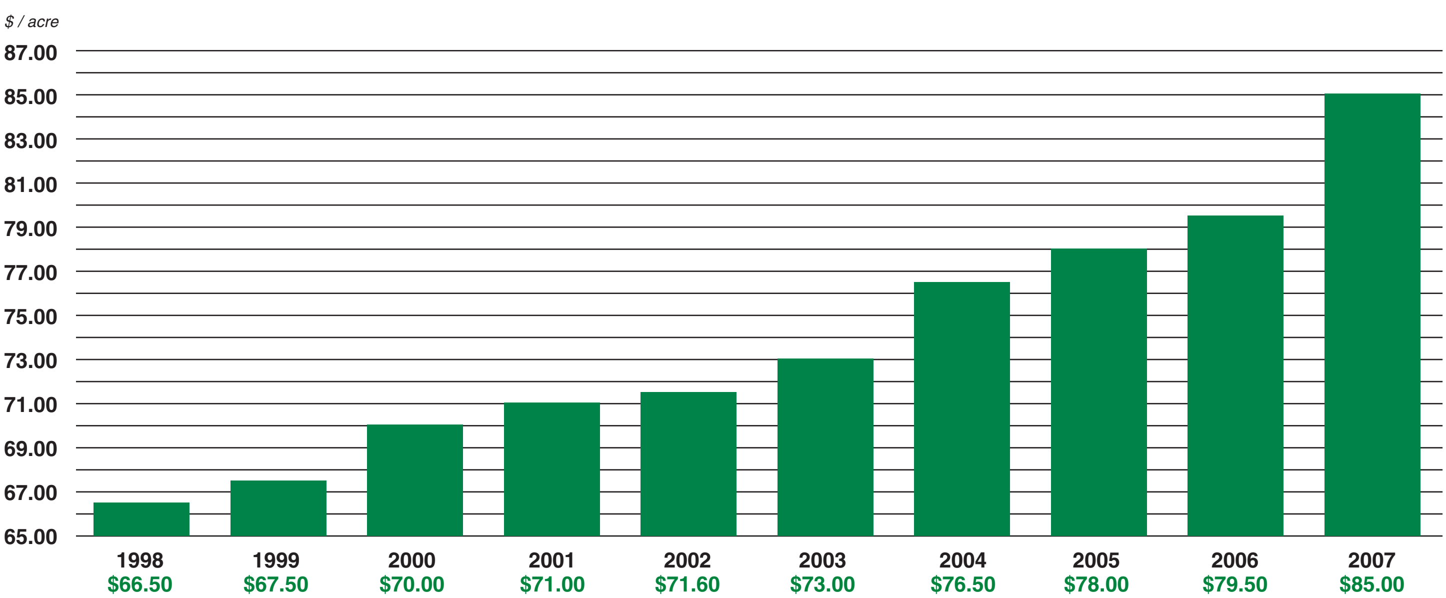
The judge agreed that Grandpa wasn't off his rocker back in the 1960s and ruled that the investment should remain in the farm. The family was initially disappointed that they couldn't shift the capital to the stock market. Today – in the longer run – the family is happy that Grandpa and the judge had the wisdom they had!

Chris A. Hurt, Ph.D., *is a professor in the Department of Agricultural Economics at Purdue University where he has teaching, research and extension education responsibilities. Dr. Hurt teaches three popular undergraduate agricultural marketing courses and conducts research related to marketing issues that affect grain and livestock farms. He also gives speeches throughout the Midwest for the Extension Service.*

As a result of his work, he has published many articles, is quoted regularly, and receives more than 200 interview requests annually. His work has received numerous state awards as well as national awards from the American Agricultural Economics Association, USDA, National Pork Producers Association, and the American Society of Agricultural Engineers.

U.S. Average Cropland Cash Rent

Dollars per Acre, 1998–2007



Source: USDA-NASS; August 2007

S&P 500 and Indiana Land Returns: 1990–2007

Year	SP 500 Annual Return + Dividends[1,5]	Cash Rent Minus Taxes[2]	Land Value Apprec.[3]	Total Return to Land[4]	Return $1,000 in 1990: SP 500 + Dividends	Return $1,000 in 1990: Total Return to Land
		Annual % Rate			Total $ Value	
1990	-2.90	5.97	5.98	11.95	$971	$1,119
1991	29.24	5.94	1.80	7.74	$1,255	$1,206
1992	7.30	6.01	1.53	7.54	$1,347	$1,297
1993	9.76	5.75	3.16	8.92	$1,478	$1,413
1994	1.33	5.56	10.35	15.91	$1,498	$1,638
1995	36.35	5.44	7.37	12.80	$2,042	$1,847
1996	22.27	5.10	14.24	19.34	$2,497	$2,204
1997	32.61	4.81	13.14	17.95	$3,311	$2,600
1998	29.99	4.55	7.91	12.46	$4,304	$2,924
1999	20.67	4.59	-2.92	1.67	$5,193	$2,973
2000	-8.95	4.51	3.87	8.38	$4,729	$3,222
2001	-11.68	4.37	4.19	8.56	$4,176	$3,498
2002	-21.87	4.28	5.21	9.49	$3,263	$3,830
2003	28.42	4.22	5.33	9.56	$4,190	$4,196
2004	10.87	4.01	7.33	11.34	$4,646	$4,672
2005	4.76	3.80	9.36	13.16	$4,867	$5,287
2006	15.32	3.57	7.37	10.94	$5,613	$5,865
2007	7.87	3.39	16.64	20.02	$6,054	$7,040
18 Year Average %	**11.74**	**4.77**	**6.77**	**11.54**		
18 Year Std Dev %	**16.68**	**0.82**	**4.96**	**4.75**		

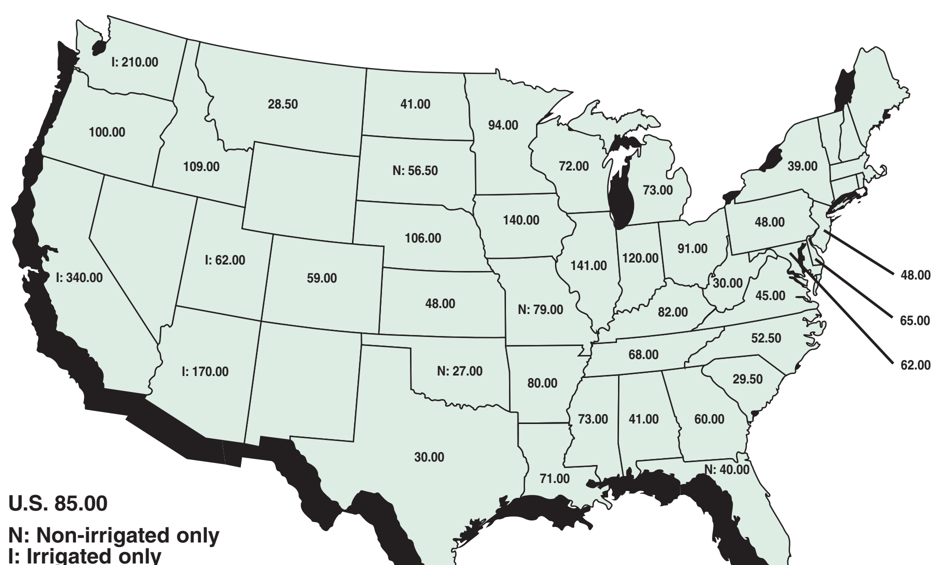
[1] Annual % change in SP 500 Index + Dividend Yield.
[2] Indiana cash rent as % of land value. (Cash rent per acre minus $14 per year for taxes, management fee, and lime costs).
[3] Annual % increase in Indiana ag land values from Purdue Survey.
[4] Total annual % return to land ownership. Sum of second and third columns.
[5] Estimate as of 12/8/2007.

The U.S. Ranks as the World's Largest Ag Exporter

The United States is now the world's largest agricultural exporter. The value of agricultural exports equals nearly one-fourth of farm cash receipts, about twice the level of the overall U.S. economy, and 1 out of 3 acres are planted for export.

2007 Cropland Cash Rent by State

Dollars per Acre



Source: USDA-NASS; August 2007

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