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# Farmland prices and the factors to watch

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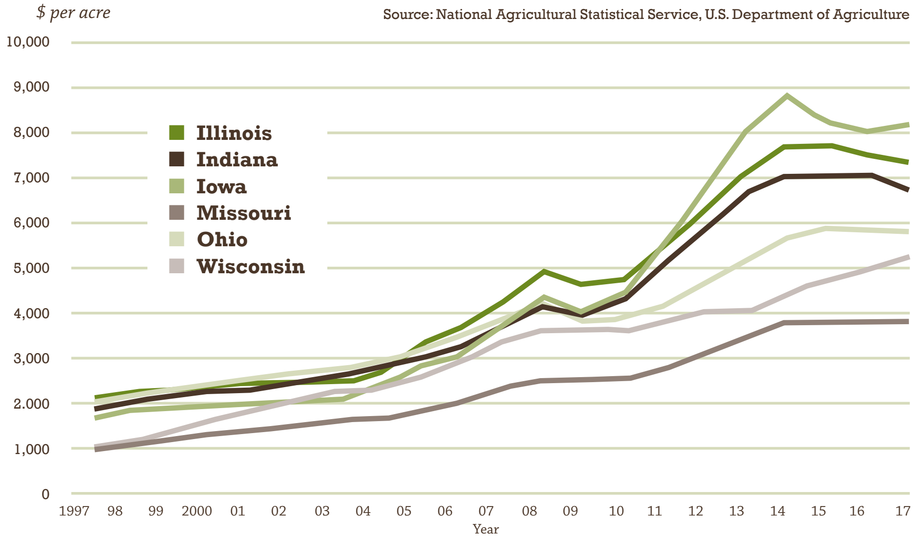
Farmland prices have been sitting on a plateau since 2014. How a handful of factors develop could cause this to change. By late spring 2018, we saw optimism that commodity prices could be higher due to projected planting acres being down. However, potential tariffs on U.S. agricultural exports to China could lead to lower farmland returns and to lower farmland prices. Interest rates likely will increase, also potentially leading to lower farmland prices.

## Farmland Prices

Across much of the Midwest, land prices increased dramatically from 2006 to 2013 (see Figure 1). Land values in Illinois increased from an average of $3,640 per acre in 2006 to an average of $7,700 per acre in 2014. During the 2006-2014 period, values increased an average of 10% per year. Similar growth rates occurred in other Midwestern states. From 2006 to 2013, average Indiana land values grew 11% per year, Iowa grew 14% per year, Missouri grew 8% per year, Ohio grew 6% per year, and Wisconsin grew 5%.

**Figure 1. Average land prices in Midwest states**

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## China's direct overseas agricultural investment has grown over tenfold in less than a decade

China's need for agricultural resources and technology and the country's sustained economic growth are driving rapid growth in Chinese investment in agriculture and food sectors abroad, according to the Economic Research Service (ERS) of the U.S. Department of Agriculture (USDA).

According to Chinese investment statistics, overseas ventures in agriculture, forestry, and fisheries soared from $300 million in 2009 to $3.3 billion in 2016. But these totals understate the magnitude of Chinese agricultural-focused foreign assets because the statistics exclude the acquisition of food processing and trading companies classified in manufacturing and service sectors, according to the ERS.

Continued on page 2

Since 2014, land values have been stable to declining slightly. From an average of $7,700 per acre in 2014, Illinois land values decreased to $7,350 per acre in 2017. During the 2014-2017 period, average land values in Illinois declined by 2% per year. During the same period, Indiana's price declined an average of 2% per year, Iowa declined by 3%, Missouri farmland remained steady. Ohio farmland increased an average of 1% per year, but that rate is much slower than the 6% annual increase from 2013 to 2017. Wisconsin is the one exception to the stability rule, increasing by 6% from 2014 to 2017. Dairy and livestock factors likely played a role in the increase in Wisconsin.

The current plateau largely has been reached due to declines in farmland returns. Returns in the future will impact farmland prices. Higher interest rates could impact the plateau as well.

## Farmland Returns

Farmland returns increased from 2006 to 2012, leading to higher farmland prices (see Figure 2). In 2005, federal legislation passed requiring ethanol to be used in the U.S. fuel supply. In the United States, most ethanol is produced with corn. The new demand for corn to produce ethanol increased corn prices, raising returns from growing corn. To maintain soybean acres, market prices for soybeans and other crops increased. Moreover, export demand for soybeans remained strong. Both, corn and soybean returns in 2008 through 2012 were high relative to returns from 1997 to 2005.

Since 2013, yields on corn and soybeans have been excellent. These excellent yields contrast to poorer yields in previous years, particularly during the drought-stricken yields in 2012. Excellent yields brought higher commodity supplies, leading to lower commodity prices and lower farmland returns.

Lower returns from 2013 to 2017 halted growth in farmland prices. At the end of March 2018, the U.S. Department of Agriculture projected lower plantings of corn and soybeans. Lower planting and near trend yields would lead to higher commodity prices and higher crop returns. Hence, there was optimism and commodity prices were on an upward path.

## Tariffs

However, pessimistic shadows almost immediately fell across commodity prices due to the prospect of agricultural tariffs. In early April, China announced its intentions to place tariffs on U.S. products imported into China. Of particular concern to Midwest landowners is a 25% tariff on soybeans.

Exports of U.S. soybeans increased during the last 20 years, with much of the growth coming as exports to China. In recent years, about 50% of the U.S. soybean crop is exported. China's soybean imports roughly equal the size of U.S. production. The primary sources of the Chinese soybean imports are the U.S. and South America. To maintain crop prices at current levels, continued growth in exports is needed.

Soybean tariffs would have a large detrimental impact on commodity prices. Over time, a tariff would cause South American soybean acres to grow, while the U.S. would shift to more corn acres. Both corn and soybean prices would fall in the U.S., leading to lower farmland returns. These lower returns then could have a negative impact on farmland prices.

Whether or not soybean tariffs occur is an open question. There likely will be ebbs and flows as tariff prospects increase and decrease.

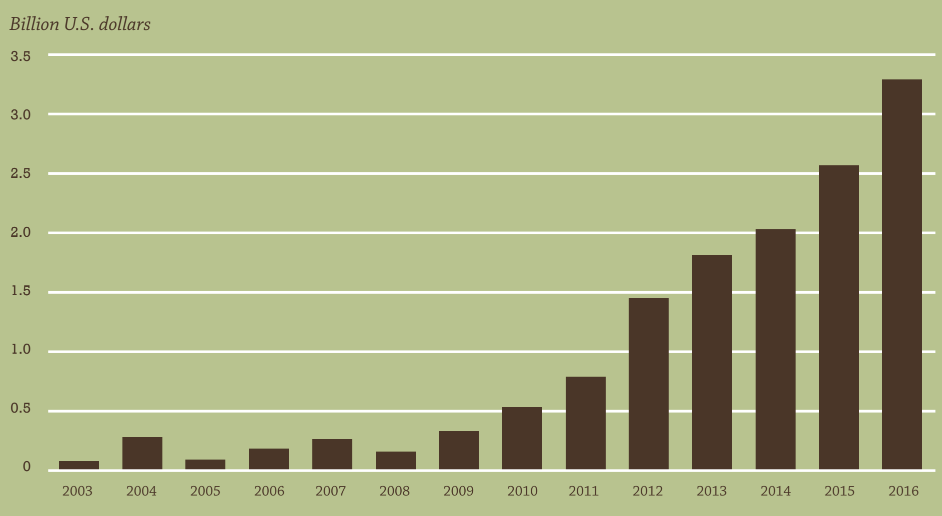
## Interest Rates

Interest rates declined through the mid-1980s to the 2008 Great Recession (see Figure 3). Lowering interest rates act to increase all asset values. Because farmland

**China's agricultural investment** continued from page 1

**An initial wave of investments during 2004-12 was focused mainly on crop production, fishing ventures, and acquiring raw materials for the Chinese market. More recently, some Chinese companies and officials have shifted the thrust of their strategy from farming overseas to acquiring established agribusiness companies based in Europe, North America, and Oceania such as ChemChina's acquisition of Syngenta and Shuanghui International's purchase of U.S.-based Smithfield Foods.**

### China direct overseas investment in agriculture, forestry, and fishing




Source: USDA, Economic Research Service using China National Bureau of Statistics data.

**Figure 2. Crop revenue less non-land costs, Heartland states, 1997 – 2017**

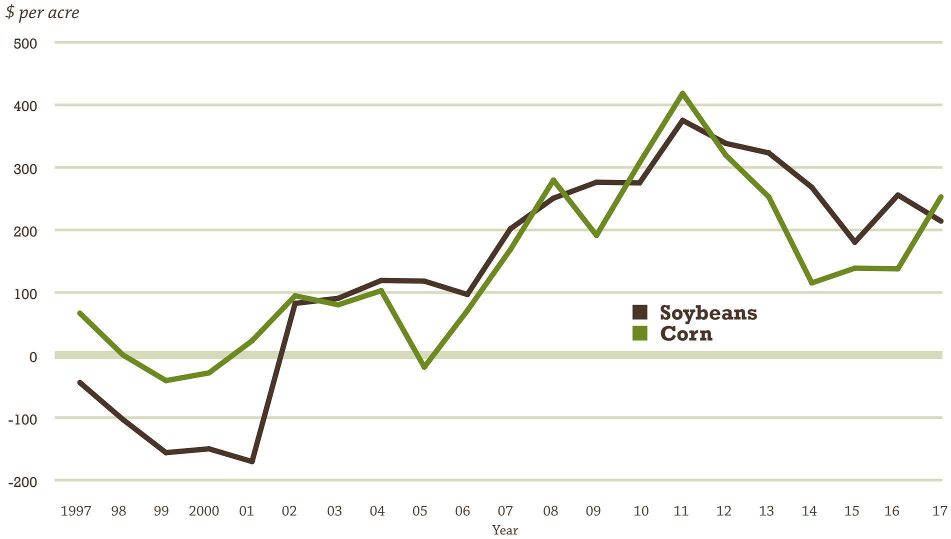



**Figure 3. Ten-year constant maturity interest rates, 1962 – 2018**


Source: St. Louis FED

should last longer than other assets, farmland is most impacted by interest rate changes. One could argue that these falling rates in previous years had as much impact on increasing farmland prices as increasing returns.

After a period of low interest rates, the Federal Reserve Bank is in the process of raising interest rates. One would expect these interest rates to soften farmland prices. However, interest rate increases are projected to be modest, likely leading to marginal impacts on farmland prices.

## Summary

As always, farmland prices will be influenced by returns and interest rates. Interest rates likely will increase, causing lower commodity prices. Farmland returns depend on the usual factors, but some optimism exists if soybean tariffs do not come into existence. The wild card is tariffs. My impression is that the probability of soybean tariffs is low, but it certainly is not zero.

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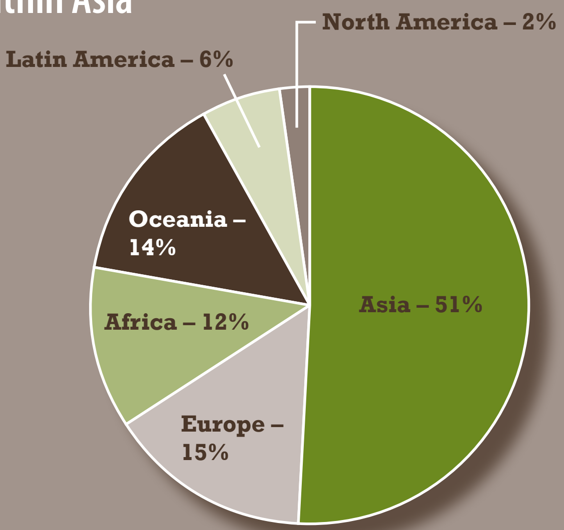
## More than half of China's foreign agricultural investment is within Asia

Chinese foreign agricultural investment has grown exponentially since 2009, according to the Economic Research Service (ERS) of the U.S. Department of Agriculture (USDA). Initial investment growth was primarily aimed at expanding access to crop production, fishing ventures, and raw materials. Most such ventures targeted eastern Russia and neighboring Asian countries, attracted by relatively cheap, underutilized land.

Chinese investments in Southeast Asia have focused on tropical crops such as palm oil, cassava, sugar, fruit, and lumber, prompted by strong domestic demand and a regional free trade agreement with the Association of South East Asian Nations (ASEAN). Asia accounts for about half of China's foreign investment in agriculture, forestry, and fishing. More recently, the strategy has moved toward acquiring established agribusiness companies around the world in regions like Europe, Oceania, Africa, and the Americas. Investment in North America, though, was limited to just 2 percent of reported foreign agricultural investment in 2014.




**China agricultural investment, by targeted region, 2014**

Source: USDA, Economic Research Service using data from the Chinese National Bureau of Statistics.

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