Land Facts
THE LORANDA GROUP, INC.
AUGUST 2013

Navigating the 2013-2014 Farmland Market

By John D. Moss, President

The USDA released their annual Land Values Summary on August 2nd and as expected the report showed an increase in farm and cropland values since 2012. In Illinois, values were up 16.9%, while in Indiana they rose 14.5% and in Iowa 17.8%. Over the next several months, the data in this report will be discussed, massaged, and analyzed ad infinitum. Ultimately, the numbers will be used to either help support or refute the theory that the land market is a large bubble ready to burst. I personally do not adhere to the bubble hypothesis, though it wouldn't surprise me to see a little air leak out in the near future either.

Looking back over the past 12 months, it's easy to conclude that the drought had the biggest impact on land prices. Lack of rain led to fewer bushels harvested, which led to higher grain prices. Add in a crop insurance program that helped eliminate much of the production risk and the result was record net farm income… income that was subsequently used to bid land prices higher. I don't think anyone could have predicted this outcome when the crops were being planted 16 months ago. There were a few other factors that helped lend support to the land market, including low interest rates and a scarcity of tracts to buy. But let's not kid ourselves, that totally unpredictable, uncontrollable, weather phenomenon known as a drought overshadowed everything.

Last year's dry weather is now a distant memory. Plentiful rainfall has many commodity traders convinced that we'll see a better harvest in 2013, and consequently crop prices are lower than in past years (see page 3). If the big harvest scenario comes to fruition and grain prices stay low, then there will be fewer dollars available for land purchases. As we saw in the fall of 2008 when grain prices softened, before buyers will aggressively bid on land they take into account not only what they have made on the current crop, but also what they anticipate to make on next year's. This doesn't suggest they won't be bidding on any land, it just means that they may be more selective and cautious on the tracts they do pursue.

Interest rates have trended up slightly the past few months, but I don't think they've moved enough to truly have a profound affect on land values in the near future. Borrowing costs remain low and the returns on alternative hard assets continue to lag, a combination that will entice outside investors to pursue farmland. As long as the Federal Reserve continues to favor lower rates, their policies should add some stability to the farmland market. I also anticipate that the supply of land will remain low, also adding stability to the market. In fact, some sales that otherwise would have taken place in 2013 were finalized last fall as many farm owners were motivated to sell their properties early in order to avoid the January 1 capital gains tax increase.

In my opinion, demand for "A" quality tracts will remain strong the next few months, unless the grain market totally collapses due to a larger than anticipated crop. Farmers and investors alike have always bid aggressively for the best land and will continue to do so. There's still plenty of cash (or land equity) in the countryside that hasn't been tapped. Farmland buyers know how infrequently land changes hands, and if a good farm comes on the market there will be plenty of bidders. I do have some concern, however, about lower quality farms being able to maintain current price levels though 2014. If profit margins look bleak next year, then it's likely that there will be fewer bidders for the lower quality tracts (i.e., those with less productive soils, poor drainage, or are difficult to farm), a scenario similar to what we saw in the fall of 2008. Even if the cash or financing is available, many farmers in uncertain times would rather delay any purchases until an "A" quality tract comes on the market. With this idea in mind, some of the best buying opportunities in the next few months may be with the less desirable parcels. The exception to this rule – if the parcel is located in an area where little has sold the past few years and there's extraordinary pent-up demand.

Forecasting land values further into the future is more of a challenge. As a farm economist recently noted, \$7.00 corn has fueled the rise in farmland prices to current levels, but \$5.00 corn may be the new norm. If so, land sellers will need to adjust their price expectations, as the net income just won't be there to support the price levels and appreciation we've grown accustomed to in recent years. Unless of course, somewhere in one of the major crop growing regions in the world there is a totally unpredictable, uncontrollable, weather condition that has a significant impact on agricultural production and grain prices again move higher.

Negotiations On the Farm…
Let the Landowner (and the Heirs) Beware

By Eric L. Sarff, Vice President

I've had the opportunity to work with a variety of landowners over the years. Most knew a lot about their property and kept current on issues involving agriculture, including lease trends and land values. Others, unfortunately, did not. Following are just a few examples of projects I've worked on recently that show what can happen when a landowner has negotiated an agreement without doing their homework:

- A "Class A" farm in East Central IL sold to an investor at a 40% discount to recent comparable sales. The seller thought at the time that the offer seemed fair, though he admitted that he hadn't bothered to ask anyone about other transactions in the area. After the fact, he wished he had.

- A client wanted to sell her farm with a lease in place. While this was possible I told her, you need to realize that the sale price might be severely discounted unless the proposed rent was at current market levels. We subsequently learned that the tenant had been paying $175 per acre, while similar farms in the area had been renting for nearly $400. The landlord had no idea that lease rates had moved up so much.

- A farmer approached and convinced his elderly landlord to sign a new lease - 8 years and at a rate that's about 50% of other comparable farms in the area. Unfortunately, no other family member knew about the agreement until they realized that they had to assume it.

The first instinct in these situations is to fault the buyer or the tenant for taking advantage of the farm owner. While there is plenty of blame to go around, the ultimate responsibility to stay current regarding market conditions still resides with the landowner. Your farmer may be the nicest and most loyal person in the world and his family may have farmed your family's land for decades, but keep in mind that when negotiating a sale price or lease terms, the other party is going to put their interests first. They don't feel obligated to confirm that you have done your necessary due diligence - in most cases, they hope you haven't. Ultimately, it's like any other business negotiation – each party is out to engineer the best deal for their side. Landowners who don't stay up-to-date on value/rent matters are putting themselves at a disadvantage in transactions involving these types of issues.

If an owner doesn't have the ability to stay abreast of current trends, either because of age or distance or some other issue, then they need to consult with or hire someone that does. It's also important to get the next generation involved to ensure a smooth transition in the future. We have worked with many clients who inherited a farm, but they had no idea what the lease terms were or even what the farm's approximate value was. This lack of involvement and knowledge can really put the heirs at a disadvantage when it's time to negotiate an agreement. Like any investment, landowners need to follow the market on a regular basis. There are too many dollars at stake not to.

The Real Estate Corner

- where Loranda addresses the concerns of Midwestern landowners.

Q - Is there any one time during the year that is best for auctioning a farm?

A - Though it is possible to auction a property anytime during the year, we have had the greatest success from October 15 thru March 15. During this time period, the crops have been harvested and the final yields are known, thus a farmer's cash flow is at its peak and he knows exactly how much he has to spend on a land purchase. In addition, with the crops removed it's much easier to view all parts of the property, an important consideration for many bidders. Farmers also seem to be more optimistic after harvest (perhaps they've been able to see the fruits of their labors realized?), an important prerequisite that ensures aggressive bidding. Finally, and most importantly, the current lease is or has expired so the buyer can assume complete control of the farm at closing. The main risk of a fall/winter sale - if grain prices dropped significantly during the 3rd quarter. While this is a possibility, we think that the other issues mentioned outweigh the commodity price concern.

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In addition to videos of many of our recent land auctions, you can now view a whole range of informational/instructional offerings, from "Farmland Marketing Alternatives" to "What Gives Farmland Value". We'll be providing even more original content in the future so make sure you stop by on a regular basis!

GRAIN PRICE ANALYSIS

Commodity prices, and ultimately net farm income, are often the best barometers to use to predict farmland price trends. The information below illustrates how volatile corn and soybean prices have been the past six years and how crucial good grain marketing can be to farm profitability.

Year	Old Crop Corn Bid on 08/01	New Crop Corn Bid on 08/01	Dec. Futures Price Range*	Old Crop Soybean Bid on 08/01	New Crop Soybean Bid on 08/01	Nov. Futures Price Range*
2014	n.a	n.a	$4.94-$5.79	n.a.	n.a.	$11.67-$12.96
2013	$5.90	$4.41	$4.64-$6.65	$13.34	$11.70	$11.45-$13.97
2012	$8.09	$7.82	$4.99-$8.49	$17.03	$16.00	$11.17-17.83
2011	$7.10	$6.51	$3.82-$7.79	$13.57	$13.24	$9.17-$14.65
2010	$3.60	$3.63	$3.43-$6.05	$10.52	$9.69	$8.45-$13.35
2009	$3.48	$3.37	$3.02-$7.07	$11.34	$9.97	$7.84-$15.54
2008	$5.14	$5.21	$2.90-$7.99	$13.42	$12.68	$7.89-$16.36

Information Source for Columns 2, 3, 5, 6: USDA-IL Dept. of Ag (Elevator Bid Report)
Information Sources for Columns 4, 7: CME Group (* Price range for the 18 months prior to the expiration of the contract)

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