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Farmland prices soar. Another bubble?

By Jim Nowlan

Forty acres of good farmland in my home county of Stark (southeast of Moline-Rock Island; west of Ottawa-Streator, Kankakee) recently sold for $11,775. Just a few years ago the land might have brought $5,000. Are we in another farmland bubble as in the 1970s, which collapsed in the 1980s, throwing many farmers into bankruptcy?

According to the Chicago Federal Reserve Bank survey, farmland prices in Illinois jumped by an average of 23 percent in just the past year. In western Iowa, prices soared by 32 percent. This is reminiscent of the 1970s, when the price of farmland tripled between 1972 and 1976.

Unfortunately for farmers who bought lots of land in the 1970s, the bubble was pricked by low commodity prices in the 1980s. An acre of good farmland that might have brought let's say $1,000 in 1981, for ease of arithmetic, plummeted to $500 by 1986.

"Two things are driving the recent high farmland prices," says land broker John Leezer of Toulon in Stark County, "the price of corn and low interest rates. The latter reduces the cost of borrowing and also makes farmland a good investment, relatively speaking."

"Farmers were more heavily leveraged (high debt to asset ratio) in the 1980s than they are today," Leezer adds. "So if there is a pullback in farmland prices in the years to come, it would not be so catastrophic as back then."

Indeed, the 2011 Farm Income Forecast by the US Department of Agriculture (USDA) reported that the average debt-to-asset ratio of 10.4 percent is an historical low.

I asked John if the talk in Washington of cutbacks in farm subsidy programs, which have buoyed farmland prices over the years, would dampen prices for cropland.

"Farmers are not nearly so dependent upon farm programs as in the past," Leezer responded, "so if the farm program goes away, there would not be a huge impact on land prices."

Net farm income for 2011 is forecast by the USDA to surpass $100 billion, a rise of 32 percent from 2010, so the bankers surveyed on land prices by the Chicago Fed expect further increases in farmland prices.

At the farmland auctions I have attended in recent months, it appears to me that the big family farmers are the ones buying the land. What is a big farm these days?

Some say that a small farmer is anyone farming less than a thousand acres and that a large family farm operation might cover 5,000 acres, about half owned by the farmer, the rest rented. Corporate farms are in the 10,000-20,000 acre range.

The increase in land prices and of corn prices has also boosted the cost of renting farmland, to as much as $400 an acre, I have heard at the local coffee cafe.

I assumed that the larger the farm operation, the more efficient it would be, but Leezer said, "Not always. There is an optimal time to plant in the spring and the window is relatively narrow. Some of the smaller farmers can do a better job of getting their planting done inside that window."

No one I know can predict the future price of corn. There are, however, some factors that suggest prices will be strong into the future. Forty percent of the corn crop goes into ethanol for blended gasoline use on highways, which is basically required by the federal Energy Policy Act. In addition, China has a rapidly growing middle class, which likes corn-fed beef. And worldwide population growth continues.

As the old saying goes, "There not making anymore of it (land)," which causes me to believe that, while there will be pullbacks from time to time, farmland prices will continue to increase over the years. Wish I owned some.