Land Prices Pinch Pipeline of New Farmers

lending agriculture

Summary: Faced with volatility in the stock and real estate markets, investors (including private equity firms) are turning to farmland as global commodity prices grow. That's keeping some people from going into farming and means that established farmers are sitting on an increasingly valuable piece of collateral. We discuss how CFIs can support existing and new farmers.

Maybe the board game Monopoly missed an opportunity by only letting players buy city lots, houses, hotels, railroads, and utilities. These days, it seems that what a lot of people want to own is farmland.

Farmland prices are at their highest value in the last 52Ys, thanks to high commodity crop prices, a strikingly robust housing market, generous government subsidies, and a long run of low interest rates. For community financial institutions (CFIs), this means that existing loans backed by farmland are even more secure than before. The pipeline for future farmers being able to finance farmland, however, may be in trouble.

High Prices for Renters and Buyers

In the US, about 39% of agricultural land is rented, and only about 1% of farmland comes up for sale in any given year, since farmland typically transfers to new owners via trusts and wills or as gifts. Both rent and purchase prices have gone up substantially.

In 2022, the national average rent for an acre of cropland was $148, up $7 from last year and higher than the previous record, set in 2015 at $144 per acre, according to the USDA National Agricultural Statistics Service. Purchasing an average acre of farmland cost $5,050; pastureland cost an average $1,650 per acre. The overall value of an acre of farmland, counting buildings and other improvements, was $3.8K, 12.4% higher than in 2021.

Multiple Factors Drive Increase

A variety of factors have driven these numbers up. Commodity crops, such as corn, soybeans, and wheat, have been robust. Next year's returns will likely be positive as well, if corn prices are between $5 and $6 per bushel, and soybean prices stay just under $13 per bushel. So far, fall 2023 bids are meeting those requirements, which is great for farmers trying to repay high loans, but drives land prices even further out of reach for new farmers.

The housing market has also been hot, with October 2022 marking 128 months of YoY increases in median US home sales prices — the longest such streak on record. Jason Henderson, a dean at the College of Agriculture at Purdue University and a former official at the Federal Reserve Bank of Kansas City, notes that this trend created a "perfect storm" for the value of farmland. *"When housing starts go up with new building construction, that puts pressure on farmland, especially on those urban fringes. That leads to a cascading ripple effect into land values even farther and farther away."*

Add a long period of historically low interest rates, bountiful government subsidies, and a volatile stock market, and many investors see farmland as a good play. Private equity firms, pension funds, real estate developers, hobby farmers, individual investors — Bill Gates is the biggest private farmland owner in the US — and other farmers all compete with anyone who wants to begin a new farm or add to one that already exists.

Where CFIs Come in

Farmland price increases mean that CFIs should take care with preserving their existing agriculture customer relationships, and find ways to work with potential new farmers that are having a hard time securing funding in order to purchase farmland.

One positive result of this development is that existing agricultural loans are quite secure. In order to support new farmers, however, providing consultation services or customized financing can help them compete against investors and private firms for the farmland that's available for purchase. Rather than rent from those firms and investors, which limits farmers' ability to expand and grow certain crops, finding ways to assist these farmers in owning their land will increase their chances to build equity and grow their business with their financial provider.

While established farmers might be reaping the rewards of high commodity crop prices, the factors that are working in their favor are creating a barrier to entry for new farmers. There is a chance that higher interest rates, which could place capitalized values below farmland prices, may put downward pressure on prices, but while the economy is still battling inflation, there is no guarantee. Without those changes, customers who want to start or expand a farm will find it difficult to do so, potentially limiting the business that they're able to bring to a financial services partner. CFIs can work to provide advisement opportunities to capture and support that new business by any means possible.

LOOKING TO GROW YOUR LOAN PORTFOLIO?

ECONOMY & RATES

Rates As Of: 02/23/2023 06:38AM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	4.84	0.14	0.42
6M	5.08	0.28	0.32
1Y	5.05	0.39	0.35
2Y	4.72	0.52	0.30
5Y	4.18	0.56	0.18
10Y	3.97	0.46	0.09
30Y	3.96	0.33	0.00

FF Market	FF Disc	IORB
4.58	4.75	4.65
SOFR	**Prime**	**OBFR**
4.55	7.75	4.57