



Tiny Bubbles or The New Land Paradigm

FEBRUARY 17, 2011

FARM CREDIT ADMINISTRATION

REGULATORS' ROUNDTABLE ON FARM REAL ESTATE COLLATERAL RISK

JAMES FARRELL, AFM, PRESIDENT/CEO, FARMERS NATIONAL COMPANY

Are High Land Values Here to Stay?

Real Estate Sales Slowed

- In 2009 and early 2010, the number of farm and ranch sales dropped
 - ▣ 25% to 35% in almost all areas



Buyer Uncertainty

- ❑ **We saw both buyer and seller uncertainty**
- ❑ **Buyers were reluctant to bid aggressively**
- ❑ **Some softening of land values**
- ❑ **Reduction in profit in agriculture**
 - ❑ **High costs and lower prices**
 - ❑ **Livestock sector losses**



Soft Markets

- **Will grain prices fall back to more normal levels**
- **Is this the top**
- **Buyers look for quality**
 - ▣ **Looking for safe haven investments**
 - ▣ **Movement away from lifestyle purchases as disposable cash reserves fell (recreational land)**



Seller Uncertainty

- **Uncertainty about the economy**
 - What are they going to do to me next?
- **Uncertainty about alternatives**
 - If I sell my land, what do I do with the money?
 - Monetary policy has had an affect
 - How would the market look today if cd rates were at 4.5%
- **Uncertainty about inflation**
 - If inflation starts up, owning land is a good hedge against it

Optimism Returned in late 2009!



Optimism Continued in 2010



- **Last quarter of 2009 & 2010 saw renewed interest in farm land**
 - **Grain prices recovered from 2008/09 lows**
 - **Input costs like fertilizer and fuel fell**
 - **Increased profit picture for farmers**
 - **Investors came back**

Land Became the Darling of the Media in 2010

- **National news stories on radio, TV and in the leading newspapers pointed out the benefits of owning land.**
 - ▣ **The Wall Street Journal ran a number of positive ag stories**
 - ▣ **This fueled investor interest**



Seller Reluctance Remained



- Possible sellers remained tight holders of land through much of 2010
 - The same uncertainties remained in the market
 - Poor alternative investments
 - Fears of inflation
 - Good profits from the land

Mid Year the Market Changed



- **June of 2010 saw a sudden increase in sales**
 - **The main increase was coming in auctions**
 - **FNC sold 40% of our volume in one quarter!**
 - **Auctions were the preferred method for many**
 - **Landowners were more willing to sell**
 - **Very high prices**
 - **Fears of capital gains**
 - **Some belief that the economy was improving**
 - **Take advantage of all time high prices**
 - **One investor is selling land and buying multi family units**

Today's Market is Changing



- **The search for quality continues**
 - **High quality farms and ranches still in high demand**
 - **Returns have dropped by 35% to 40%**
 - **Lesser quality farms are gaining some momentum**
 - **Buyers are attracted to the better returns**
 - **Prices are starting to increase on the lower quality units**

Who's Buying?

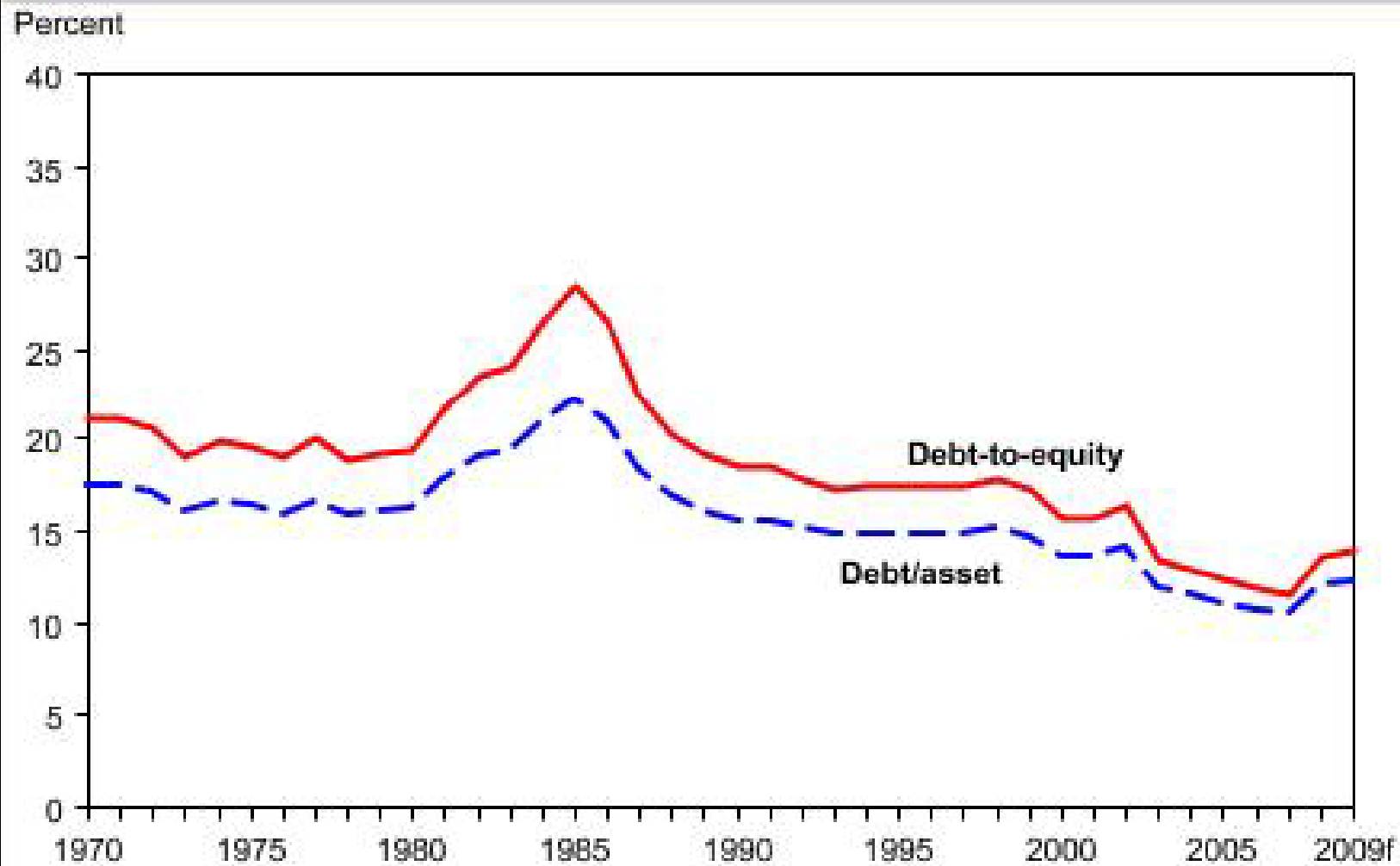
- **Through May of 2006, 1031 money was pushing this market**
 - **There is little 1031 money today**
- **Today cash is coming into the market, as the return for cash is minimal**
- **Three types of buyers today**
 - ▣ **Farmers operators**
 - ▣ **Traditional investors**
 - ▣ **Non traditional or new investors**



Buyers Defined

- **Farmers are spending profits, and expanding**
 - ▣ **They are spending cash, but they are also leveraging land they already own**
 - **Maybe 40 to 45% of sales have leverage**
 - ▣ **The margins are getting thin**
- **Two types of Investors**
 - ▣ **Those who currently own land and like the asset**
 - **Add on acres, generally low leverage**
 - ▣ **New investors**
 - **Bullish on ag**
 - **Will leverage**
 - **Plan to hold for 10 years**
 - **Often little ag knowledge**
 - **3.5% to 3.75% returns**
 - **Few foreign buyers**

Farm sector debt-to-equity ratio, 1970-2009f



f = forecast.

Source: Economic Research Service, USDA.



Who's Selling?

- **Farm Operators don't generally sell land**
 - **Consolidation or forced sale generally**
 - **Recently some are selling to take advantage of the high price, with a 3 to 5 year lease back**
- **Non operating owners are the sellers**
 - **Demographically, 75% to 80% are over the age of 65**
 - **Most sellers have inherited at least some if not all of their land**
 - **In our client mix, client sales have dropped by over 40% over the last 2 years**

Land Transactions

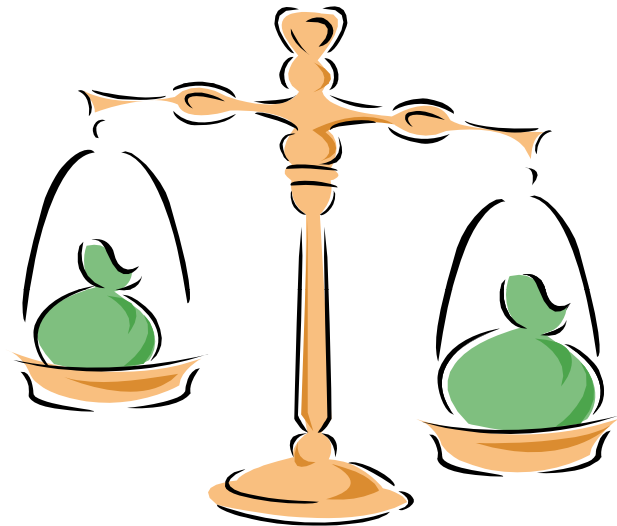
- **We sell about 35% at auction**
 - ▣ **Top prices received at auction today**
 - ▣ **Less of a stigma when selling at auction**
- **Estimate – 1/3 of the land sold is a quiet sale**
 - ▣ **Not on the market, sold at a discount**



Appraised values are often below auction values.

Cash vs. Financing?

- **Hard to quantify**
 - ▣ **My estimate, over 45% of transactions have some financing**
 - ▣ **Two major lenders noted**
 - **Regional lender estimated 25% to 60% of sales financed**
 - **National lender estimated 60% of mid west sales financed, and 90% of Mid South sales financed, all CA sales have some finance**



Is This a Bubble?

- **A case can be made that it is a bubble**
 - **Record investment in hedge funds**
 - **This is at least in part the reason for strong commodity prices**
 - **Market cycles have been shortened**
 - **A lack of safe alternative investments leaves landowners who might sell sitting on the side line while those with cash try to buy land as a safe investment and hedge against inflation**
 - **Is cheap money part of the cause?**
 - **Returns are not keeping up with price increases**
 - **All ag costs are increasing and margins are thinning**

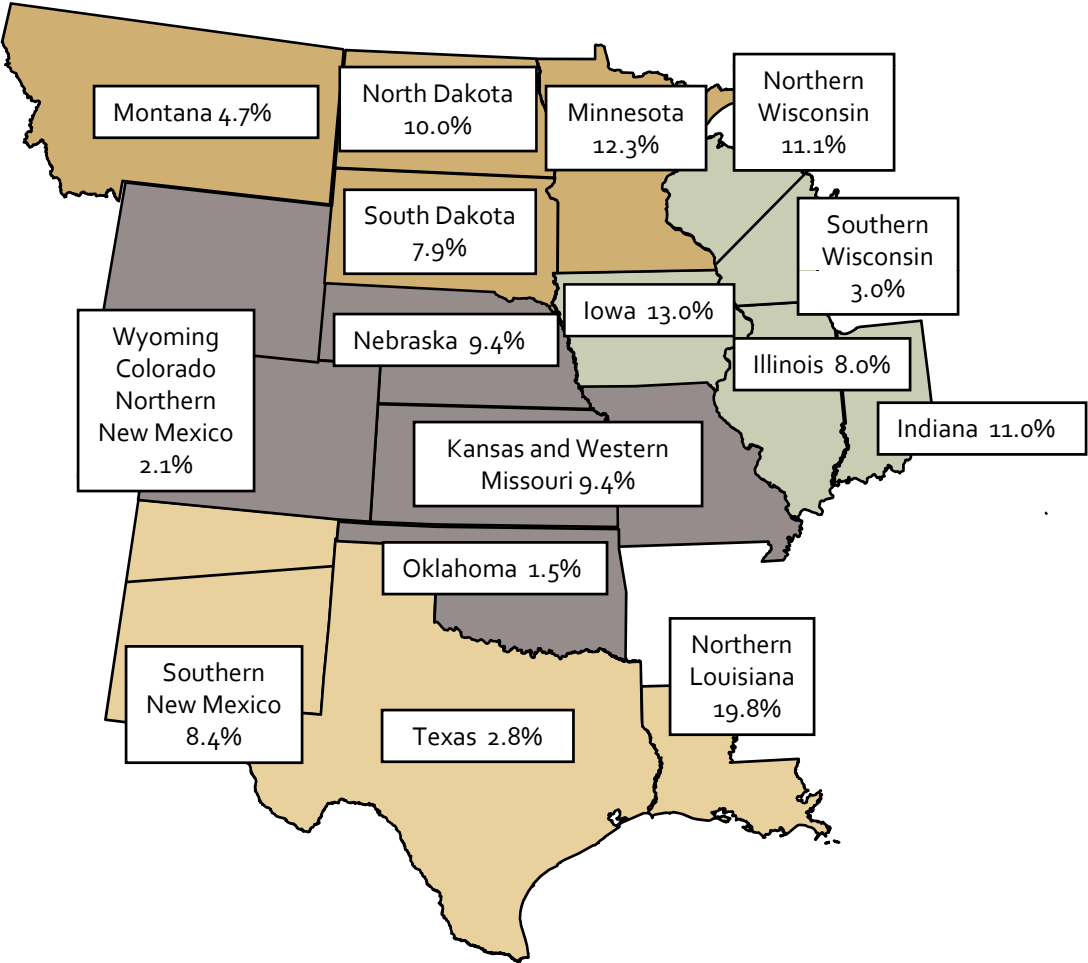
So How Strong is the Market?

- **Year over year changes from Federal Reserve Bank surveys**
- **FNC agent survey information from September**
- **Some sales from around our service area**



Good Quality Farmland (Non-irrigated Cropland) Values

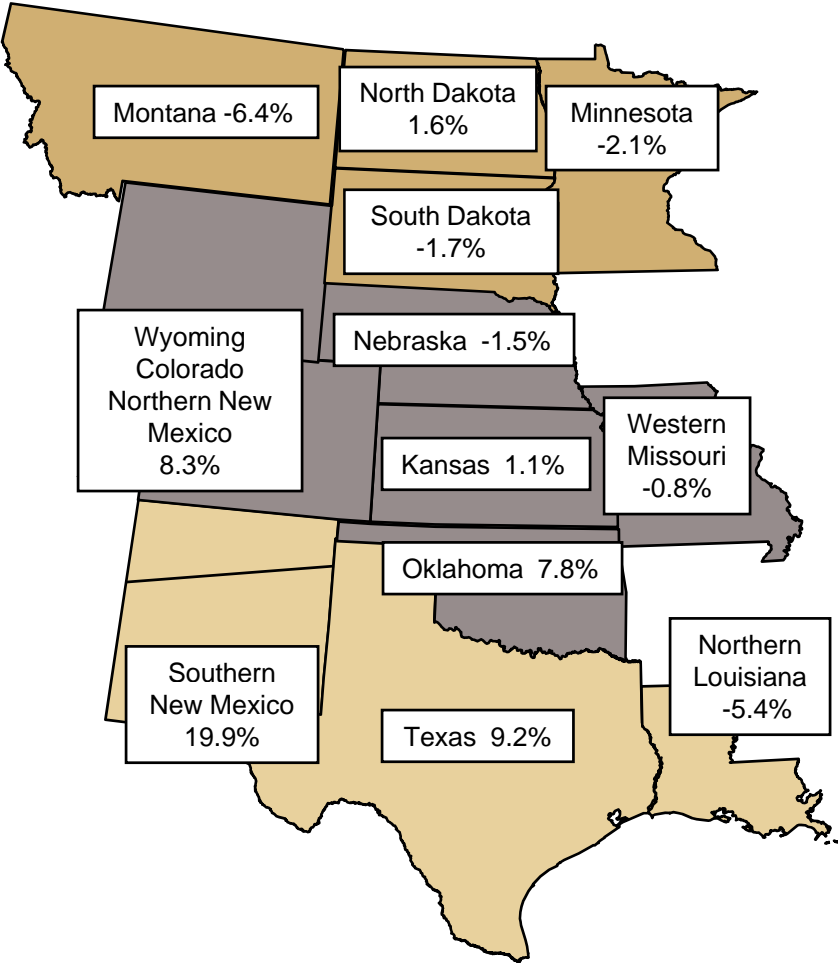
(Percent change Third Quarter 2009 to Third Quarter 2010)



Source: Federal Reserve District Surveys (Chicago, Minneapolis, Kansas City, Dallas)

Ranchland – Change in Value

Second Quarter 2009 to Second Quarter 2010

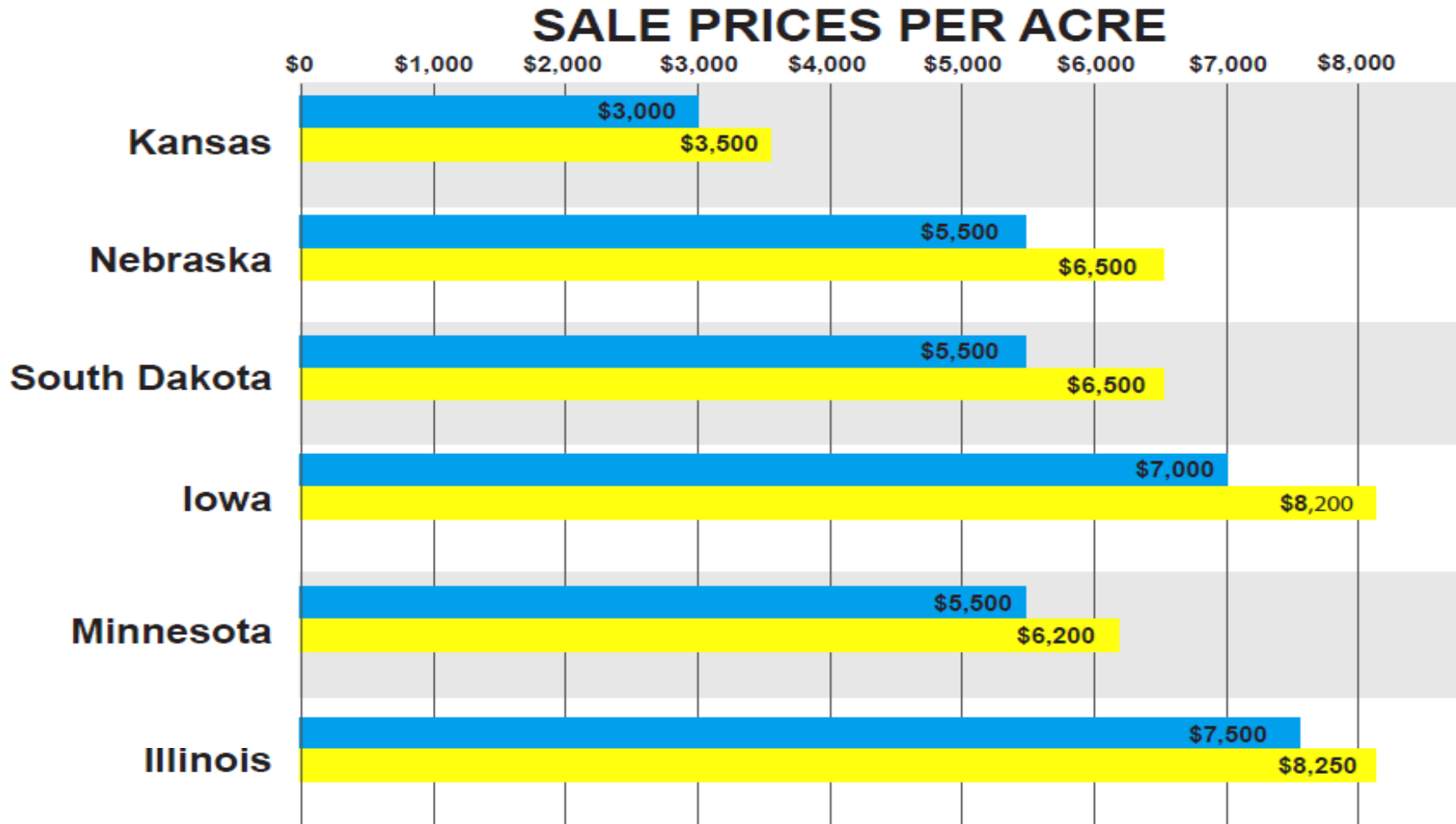


Source: Federal Reserve District Surveys (Minneapolis, Kansas City, Dallas)



Cropland Values by State

As of 1/1/2011



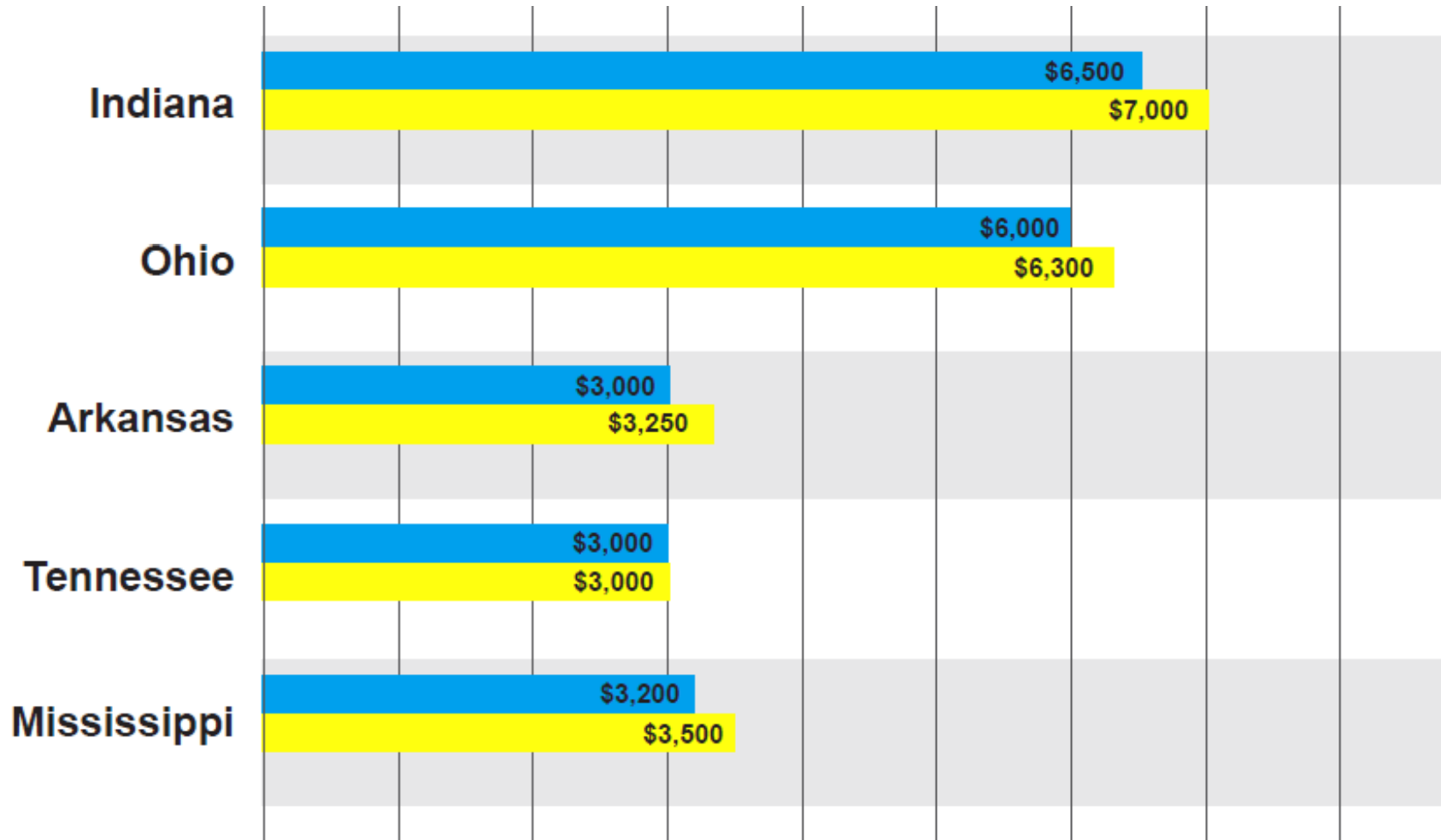
Source – Agent Survey

■ June 2010 Value – ■ December 31, 2010 value



Cropland Values by State

As of 1/1/2011



Source: Farmers National Company Agent Survey

June 2010

December 2010

Recent Sales Data

- **A look at some recent auctions around the FNC Service area**
- **We sold over 650 farms in fiscal 2010, just over \$300 million of land**
 - **Nearly all sales are on our website – www.farmersnational.com**



Select FNC Area Sales



- **January 2011 sale 158
Ac. Wright Co. IA
\$6,875 per acre**
- **December 2010 sale
160 Ac. Holt Co. NE
\$4,350 per acre**
- **Dec. 2010 sale 134
Ac. Freeborn Co. MN
\$5,500 per acre**
- **Feb. 2011 sale
79.2 acres Christian
Co. IL
\$9,100 per acre**

Strong Markets Most Places

□ Dec. 2010 sale 78
acres Montgomery Co.
IA \$6,350 per acre

□ Dec. 2010 sale 160
acres Nuckolls Co. NE
\$6,600 per acre

□ Dec. 2010 sale 800
acres Bourbon Co.
KS \$1,625 per acre

□ Dec. 2010 sale 226
acres McLean Co.
IL \$8,335 per acre

Record Demand

□ **Dec. 2010 sale**
Benton Co. IN 68.6
acres \$7,575 per
acre

□ **Nov. 2010 sale**
Jackson Co. MN 160
acres \$6,875
per acre

□ **Nov. 2010 sale Clark**
Co. SD 400 acres
\$4,275 per acre

□ **Nov. 2010 sale**
Marion Co. MO
426.2 acres \$5,425
per acre

Mid South Sales

- **Leflore county,
Mississippi**
 - **May 2010**
 - **584 acres, 519 tillable**
 - **Irrigated, precision
leveled**
 - **Sold \$2725 per acre**



More Mid South Sales

- **Pulaski County Arkansas**
 - **June 2010 sale**
 - **2760 acres, 2486 tillable**
 - **Sold \$2835 per acre**
- **1206 Acres – Ochiltree county, TX**
 - **August 2010 sale**
 - **\$509 per acre**
- **Chicot county Arkansas**
 - **February 2010 sale**
 - **878 acres, 838 tillable**
 - **Sold for \$3,376 per acre**

Tiny Bubbles . . . ??

- **Bubbles are in select areas**
- **We will need to have an increase in velocity to trigger the pop**
 - ▣ **something will need to happen to convince owners that the market will drop or they will hold if values fall**
 - **Short term capital needs?**
 - **Stronger dollar, lower grain prices**
 - **Interest rate increase**
 - **Would a 4.5% cd affect the land market?**



Looking Ahead to 2011 and Beyond



- **Land values will remain strong for the first half of the year**
- **Demand for land will remain strong**
 - ▣ **As long as we can maintain good grain markets**
- **Investors will continue to move to the fringe areas of the Mid West**
- **Demand for the more marginal land will increase some, as will the values**
- **When will interest rates rise?**

**IN THE MEANTIME – IT IS A
GREAT TIME TO BE IN
AGRICULTURE!**

