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IFES 2016: Farmland Leases: A Reset Needed

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This is a presentation summary from the 2016 Illinois Farm Economics Summit (IFES) which occurred December 12-16, 2016. A complete collection of presentations including PowerPoint Slides (PPT) and printable summaries (PDF) are available here.

Higher farm incomes that began in 2007 and continued through 2012 resulted in significant increases in cash rents. Summary data from the Illinois Farm Business Farm Management Association (FBFM) records for this time period indicated that operator's total net farm income, except for 2009, averaged over $200,000. During the previous ten years', total net farm incomes averaged well below $100,000 per farm. Incomes in 2013 and 2014 were about one third of the 2012 total net farm income and the 2015 income figure was basically a breakeven amount. Projections for 2016 and 2017 do not indicate any significant improvements in net farm incomes. Selected data indicate that average cash rents have started to decrease. But what are appropriate cash rent levels given today's economic environment?

Cash rent leases make up a significant percentage of the land that farm operators lease. According to the FBFM records, for the State of Illinois, 43 percent of the land farmed is cash rented, 34 percent is crop shared and 23 percent is owned. The FBFM data indicate that changes in lease types have slowly but steadily been moving from crop share leases to cash rent leases. According to a survey of members of the Illinois Society of Professional Farm Managers and Rural Appraisers (ISPFMRA), for 2015, 42 percent of their leases were crop share leases and 51 percent were cash rent leases. Less than 7 percent were using custom farming arrangements. Of the 51 percent of cash rent leases, 31 percent of all leases were traditional fixed cash rent leases and 20 percent were variable cash rent leases.

According to the USDA, average cash rents in Illinois increased from $141 per acre in 2007 to $212 in 2012, a 50 percent increase. Average cash rents continued to increase in 2013 and 2014 even though farm incomes declined, averaging $223 and $234 per acre respectfully. Another source of cash rent data, survey information from the ISPFMRA, indicate that the mid one-third average rent for excellent farmland averaged $183 per acre in 2007 and increased to $379 per acre in 2012, a 207 percent increase. The mid one-third averaged $396 per acre in 2013.

According to the USDA and ISPFMRA data, cash rents have started to decline. The USDA data indicated the average cash rent for Illinois for 2016 was $221 per acre. But this is only $13 per acre less, or a 5.6 percent drop from the 2014 high of $234 per acre. According to the ISPFMRA data, cash rents peaked in 2013. The mid one-third average cash rent for excellent land was $396 per acre and for good land was $339 per acre. The average cash rent for excellent land for 2016 dropped to $325 per acre, a $71 per acre or almost 18 percent drop from the peak. Projections for 2017 are for another $24 per acre drop.

Cash rent for good land dropped to $283 per acre in 2016, a $56 per acre or a 16.5 percent drop from the 2013 high.

The most recent University of Illinois crop budgets and projections for 2016 indicate that for central Illinois highly productive land, the operator and land return for corn is $240 per acre and for soybeans $335 per acre. The average for a 50/50 corn soybean rotation then would be $288 per acre. According to the ISPFMRA data, the majority of their rents would be above this level for 2016. The initial budget projections for 2017 using trend yields and corn and soybean prices of $3.50 and $9.10 respectively would result in lower returns in 2017 then 2016. This indicates that there will continue to be pressure to lower rents at a more rapid pace then has been the case so far.

One of the challenges with a fixed cash rent lease is determining an equitable or “fair” cash rent amount. Many times leases are negotiated and set in the fall or winter ahead of the year of the lease. At that time, yields are unknown and crop prices can change considerably from the time the lease is signed until when the crop is marketed. Given this challenge, flexible or variable cash rent leases are becoming more popular. Generally, these leases will take into account actual revenue generated (prices and yields) in determining a final cash rent amount. A base or minimum rent is determined and an additional rent amount can be paid if revenue exceeds a certain amount or the final rent is determined as a set percentage of the gross revenue. A flexible cash rent lease can more accurately determine a cash rent amount given the actual farm profitability for the year but there are still terms of the lease that need to be negotiated. These include but are not limited to items such as what is the base or minimum rent and what are the factors that adjust the rent and how are these determined.

Additional Resources

The slides for this presentation can be found at:

http://www.farmdoc.illinois.edu/presentations/IFES_2016

For current agricultural land rent information, see:

http://www.farmdocdaily.illinois.edu/

For other information on farmland leasing, see:

http://www.aglease101.org/DocLib/default.aspx#LeasePubs

http://www.extension.iastate.edu/agdm/

https://ag.purdue.edu/commercialag/Pages/Resources/Farmland.aspx

https://www.agmanager.info/land-leasing/forms