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Farmland Prices and Bubbles

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The Illinois Society of Professional Farm Managers and Rural Appraisers released their annual farmland values report in Bloomington on March 16, 2011 (see www.ispfrma.org for order form). Between January 1, 2010 and December 31, 2010, farmland values increased substantially over Illinois, with variability in increases across regions and farmland qualities. Farmland increased by 14 to 18 percent for northern Illinois and 10 to 20 percent in central Illinois. Higher increases were noted in southern Illinois. Illinois Society results suggest an overall increase of 15 percent in Illinois farmland prices.

This Illinois Society report confirms increasing farmland price reported in the AgLetter, a publication of the Federal Reserve Bank of Chicago. According to the Chicago FED, land values in northern and central Illinois increased by 11 percent during 2010. The 11 percent compares to a 6 percent rate average from 1965 through 2010. The 11 percent increase in 2010 was the third highest increase since 2000, exceeded by increases in 2007 (15 percent) and 2004 (13 percent).

The 2010 farmland price increases are attributed to continuing low interest rates and higher returns to farmland. Corn and soybean prices began reaching higher levels in June and July of 2010, causing higher returns to farmland. Higher farmland return then caused increasing farmland prices during the second half of 2010.

Increasing farmland prices have led to concerns about farmland price bubbles. For example, the Federal Deposit Insurance Corporation (FDIC) held a conference on March 10th entitled “Don’t Bet the Farm: Assessing the Boom in U.S. Farmland Prices” (see http://www.fdic.gov/news/conferences/2011-03-10.html). At that conference, however, speakers indicated that it were unclear whether farmland prices have reached the bubble stage. Joe Glauber, chief economist of the U.S. Department of Agriculture, noted that while farmland values rose sharply over the past five years, comparisons to the late 1970s seem unfounded. Brent Gloy, associate professor from Purdue, indicated: “It is not clear to me that on balance land is overvalued at present”.

As always, events could cause farmland prices to decline. Whether probabilities of such adverse events occurring are higher now is an open question. As anyone familiar with agriculture knows, agricultural returns are subject to change, almost without notice. Also, interest rate increases could occur, leading to lower farmland prices. Brian Briggeman, an economist of for the Federal Reserve Bank of Kansas City, noted at the FDIC conference that interest rate risk is high for farmland values.

Interest rate risk is high. This risk, however, was not created by farmland market participants. Rather, it was created by the FED. Since 2008, the FED has followed a policy designed to lower interest rates through measures like quantitative easing. These low interest rate policies have the general effect of raising not only farmland prices, but all asset prices including stock prices, real estate prices, and commodity prices. However, which assets are in the bubble stage is difficult to determine. Perhaps FDIC should discuss their concerns about farmland price bubbles with their sister Federal body, the FED.