September 4, 2015

THE MARGIN SQUEEZE

Tina Barrett, in a Nebraska Farm Business newsletter, recently said "Cash Rent Increases: When is the Right Time to Give up a Lease?" From 2005 to 2014, on average irrigated cash rents more than doubled for corn ($127.71 to a peak of $274.74 in 2013) and now accounts for 31% of the total cost of growing irrigated corn on many farms. It's no wonder, that in times of narrow margins, farmers are considering ways how to reduce expenses and deal with cash rents.
To be fair, landlords are dealing with higher taxes that followed the increased land evaluation wave. The average personal property and real estate taxes per acre has increased. In the same 10 year period, real estate taxes have increased from $29.22 per acre to $55.71 per acre according to the Nebraska Farm Business Association.

It's hardly anyone's desire to work all year knowing you will lose money on a specific cash rent farm, but giving up farm ground is a long term and often emotional decision. As a friend from college reminded me this past weekend, it's a lot about timing and inheritance too. His margin is different what he can afford to pay for cash rent compared to a farm operation with a fair amount of owned land free and clear.

Nebraska farmers, among others, are experiencing a new cost-price squeeze unlike that of the farm crisis of the late 1970's to the mid 80's. During that farm crisis, interest rates, reduced crop demand and rapid land devaluation financially pressured many leveraged farmers.

The current farm profitability squeeze is different. Current interest rates are near historic lows, debt exposure for most farmers is low and corn demand is consistent due to the domestic ethanol and the Nebraska beef and animal industry.

What's causing stress locally is lack of rain in August on many of our dryland farms which will lower production and our costs are not yet aligning with revenues. Cost control will be a critical factor in survival the next few years. Input costs such as land costs, seed, fertilizer and machinery, rose rapidly in the last few years, but have not begun to decline yet.

Gary Schnitkey, University of Illinois Ag Economist, says that costs only drop back by 18% from their peak and take several years for the adjustment declining on average 4% annually looking at our past history. When reviewing your costs in 2015, ask yourself whether the money invested is giving a return above cost. Some things may make sense to do at $7.00 corn when the return doesn't exist at $3.50 corn. When looking at the return, look to data that is trustworthy and not testimonials about a product. You can only analyze returns using reliable data. Rental arrangements will be re-negotiated, they will have to be.

Early detection of financial stress allows farm and ranch managers time to make adjustments before the situation is too serious to correct. Robert Tigner, an extension educator and economist, says "early recognition, early resolution." He has a good blog and some good ideas including a link to a new article from Texas A&M about future business expansion opportunities on our horizon at: https://redwillowfarmranch.wordpress.com/

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