Transitioning America’s Farmland

John L. Taylor, National Farm & Ranch Executive, U.S. Trust, Bank of America
Private Wealth Management

According to the USDA’s 2007 Agricultural Census, the average age of the American farmer was 57.1 years old and the fastest-growing age segment was 65+. Consider these additional supporting data:

- 32% of American farmers were 65 and older, while another 32% were between ages 55 and 64.
- A total of 64% of America’s farmers are age 55 or older.
- The number of farmers age 75+ grew by 20% between 2002 and 2007.

It’s clear that over the next decade or so, much of America’s farmland – now held or farmed by an aging generation – will need to be transitioned. How this will happen is not easily answered due to a number of factors and changes that have occurred over the last two to three decades.

While granular data are not so easy to come by, I can speak to this matter as an aging baby boomer who grew up as the son of an agricultural implement dealer in western Texas (who also farmed on the side).

Our Background
U.S. Trust has been managing farms and ranches for well over 50 years. Today, we are one of the largest fiduciary managers of farms and ranches in America. We are fortunate to have 16 full-time farm or ranch managers, most of whom come from 2nd-, 3rd- or 4th-generation farming or ranching families. All have degrees and experience in agriculture. We are going to share with you some firsthand observations of the many trends that bring us to where we are today.

TECHNOLOGY
A key trend over the last 10 to 15 years has been the tremendous advances in agricultural technology. The tractors and equipment used to be much smaller — most being four-row equipment. As I moved through high school, four-row quickly gave way to six- and eight-row. Word had it that twelve-row was on the way. Tractors began to come with cabs, featuring both heating and air conditioning, almost like cars. I still remember my dad scratching his head after visiting some of the John Deere plants and wondering how much further things would go.
We have come a long way since those days of the early 70s. We now have 48-row planters and tractors have on-board GPS capabilities, computers and monitors. We have variable application rate technology utilizing downloadable soils maps, which enable constant monitoring of inputs and outputs. Many farmers have laptops in their trucks, as well as systems back at the farm. They can use their data to provide financial analysis, production modeling and much more.

Indeed, farming has moved into the modern age. I have watched it grow from a trade to a true profession with all of the sophistication and specialization of many other industries. New technology in seeds – including genetic modifications to help with weed and pest control, drought tolerance, lower water and fertilizer needs – has emerged, as have new and more sophisticated agricultural chemicals.

“When I grew up, most farmers had only four-row planters and combines with four-row corn heads; so 300 acres was a full-time job. Today, most planters are at least 16- or 24-row; and most combines have either 8- or 12- row corn heads and 40 ft. wide grain heads. Other major technological advances – like GPS systems and Ag Precision computer and record-keeping programs – enable farmers to vary the application rates of fertilizer as the implement moves across the field. And today’s planters are sophisticated enough that they can couple with GPS systems and adjust the number of seeds planted per acre based on soil type in that specific part of the field. Because of these technological advances, farms have grown to as much as 6,000 acres in just 10 years.” — Bob Frizell, Senior Farm & Ranch Manager, Des Moines, Iowa

“The evolution of farm machinery and implements over the last quarter century has enabled farmers to increase efficiency at least four- or fivefold. I remember the early cotton harvesting machines would at most cover maybe 10 acres a day, whereas today they can easily cover 60 or more acres daily and provide real-time harvest data.” — Tommy Funk, National Farmland Acquisition Manager, San Antonio, Texas

EDUCATION

No surprise, the knowledge a farmer must possess today is much different than it was in the past. When I graduated high school, many in my class began their farming careers with their dads. Most had been helping for several years anyway, and it was very similar to an advanced apprenticeship. What we see today is that younger farmers typically have some college education. A growing number have agricultural degrees, and many have taken some business courses as well.

We have directly observed this trend over the past 10 years as the tenants to whom we lease much of the farmland we manage to fit into this category. Young farmers embrace the new technology and seem to be pushing it as well. Gone are the days of note pads in the shirt pocket and pencil calculations of application per acre, yields and inputs. Instead, tablets, laptops and an increasing number of smart phone apps crunch data from many sophisticated systems that are now crucial components of much of the farming equipment today.

“A lot of older farmers have no interest in retiring and traveling. They’re going to work as long as they can. But these farmers and their families do recognize the need for transition. That’s why the adult children are educating themselves, getting solid work experience and then returning to the family farm to help their parents with the operation and learn how to eventually run it themselves.” — Mary Jane Rozypal, Regional Farm & Ranch Manager, Houston, Texas
ECONOMICS AND SCALE
Tractors that used to cost $35,000 are now $250,000 and up. Combines may well be $300,000 or more. Add in planters and other implements, and you quickly have more than $1,000,000 worth of sophisticated equipment that will allow farmers to tend much more acreage than they could have 20 years ago. But those higher equipment costs have also enabled a notable increase in scale.

According to the USDA Agricultural Census data regarding Harvested Cropland Farms, in 1974 there were 32,752 farms of 1,000 acres or more. By 2007, the number of Harvested Cropland Farms of 1,000 acres or more had more than doubled to 80,821 farms. This increase in the number of larger farms is not really surprising, given what we have already discussed.

The amount of acreage a modern tractor with a 24-, 32- or 48-row planter and a combine can handle is much different from the equipment of yester year. I often find it surprising when I hear about the disappearance of “small family farms.” What most people don’t understand is that with the cost of equipment today farmers can, and must, farm larger blocks of acreage to pay for that equipment and make a profit. There are still many family farms. They’re just a lot bigger than they used to be. Unfortunately the smaller farms of days gone by simply cannot be operated economically and support a family without an additional source of income.

It appears this aggregation of farm acreage has actually helped transition some smaller farms over the last decade or so. Those farmers who had enough scale and capacity to invest in newer equipment and technology either bought or leased additional acres to add to their farming enterprises. This further explains how the number of farmers in America has decreased. We have moved to fewer farmers using better equipment to scale up their operations and become more efficient.

But, as we noted at the start, many of these farmers are now in their 60s and beyond. The question remains, “How will this land be transitioned to the next generation of American farmers?”

“Today’s higher land prices, along with the need for additional acreage, have made leasing a popular – and necessary – opportunity for farmers. That’s enabled investors to find a market in leasing to savvy farmers who prefer to leverage their liquidity for leasing additional land and farming it more efficiently with high-tech machines that maximize yields.” — Jeané Redmond, Regional Farm & Ranch Manager, Kansas City, Missouri

“We’re seeing a new phenomenon now called ‘generation skipping,’ and my Dad’s farm – where I grew up – is a great example of it. When I had the opportunity to take over for my Dad in the 80s and 90s, times were hard. Farms could barely make enough income to support one family, let alone two. So my Dad has continued farming the land on his own to this day. Now at 75, he’s looking to transition his operation to our family’s next generation — my nephews, who are seeking additional acres to farm, so they can leverage my Dad’s equipment for more efficient production and compensate him for use of those machines.” — Kevin Lickteig, Senior Farm & Ranch Manager, Kansas City, Missouri

OLD MODEL VS. NEW MODEL
Looking again at some high-level survey data from the USDA – as well as what we see from the farmers we work with across the nation each day – the general rule in the past seemed to be that most farmers owned the majority of the land they farmed. According to the USDA 2007 Agricultural Census, 77% of farmers 65 and older owned all of the land they farmed. In contrast, only 59% of farmers 45 and younger owned all of their land. We also see fewer children coming back to take over or join the family farm operation. Clearly some still do, and there has been an increasing awareness the last few years about transitioning land to future generations. However, for those farmers whose children decided to pursue other careers, transition is a concern that we believe will intensify in time.
No one can argue that farmland has seen tremendous appreciation over the past 10 years. We believe much of this is attributable to an overall increase in demand brought about by increased world population and – more importantly – per capita GDP growth in many emerging economies, such as China, India and other regions of Asia. This has allowed a large segment – often referred to as the emerging middle class – to consume more grains, as well as more protein in the form of meat from livestock, which in most cases uses grain as the precursor feed stock. This increased demand for grains and other food has driven up prices, which in turn drives up the gross income a farmer can make per acre. That of course ultimately results in an increased price per acre of farmland that produces more gross income than in the past.

With increased land values, what a farmer owns today may well represent the bulk of his or her net worth and estate. The old model of owning land and the equipment needed to work the land no longer seems to fit. One of the lessons learned from the crash of farm prices in the 1980s was that a lot of leverage is never a good thing. The result is that we are seeing a new model emerge in which farmers tend to own less of the acreage they farm. As we noted above, the high costs of equipment required to provide a reasonable quality of life for their families means that farmers need to farm more acreage with lower overhead costs than in the past. Similar to businesses that do not own – but lease – the buildings they occupy, it may be that farmers also choose to invest their capital in equipment and technology rather than in land ownership. We believe more and more they may choose to lease the land so they can farm at a scale that allows them to be profitable and not have escalated debt levels.

**ONE SOLUTION — BASED ON OBSERVATIONS FROM THE PAST FEW YEARS**

Over the past six years or so, we have seen an increasing appetite for farmland as an investment; and we offer this asset class as a portfolio diversification strategy to our clients. In a number of cases, we have purchased land from farmers who were selling and retiring for our clients. We then leased that land to many of the next-generation farmers we mentioned above, allowing them to grow their operations without saddling themselves with huge amounts of debt, while providing a net return to the investor buying the land.

In other cases we’ve purchased land for clients from farmers looking to transition into retirement and then leased the land back to the farmers who we purchased it from. This is a win-win; because it allows the farmer to take advantage of increased land values, monetize the value of the farm and begin some estate planning. It also gives the farmer more control, facilitating additional years of income with lower overhead and more asset liquidity, securing retirement funds and enabling more choice of when to retire.

Of course, each situation is unique; but the facts are clear. American farmers are getting older, and many don’t have a succession plan in effect for when they’re ready to retire. It is vital to our nation that educated, professional farmers and agricultural investors work together to keep America’s agricultural industry stable and strong. By connecting investment capital, farmland and this next generation of young farmers, we believe America can continue its historic role as the leader in world agriculture.

**FOR MORE INFORMATION, CONTACT YOUR U.S. TRUST ADVISOR TODAY.**

“In my home county during the early 80s, the average farmer worked about 1,100 acres and owned 50% of that land. Today, I’d guess that the average farmer has more than doubled the size of that operation and would – at most – own only 25% of the land. You can buy land or machinery, but it is really hard to buy both. And it is much easier to increase cash flow by unloading land overhead costs, switching to a land-lease model and investing in high-tech efficient equipment that enables the production of high-yielding crops at prices that compete in the global marketplace.” — Kevin Paulson, Regional Farm & Ranch Manager, Spokane, Washington
The information and views contained in this publication are for informational purposes only and do not provide investment advice or take into account your particular investment objectives, financial situations or needs and are not intended as a recommendation, offer or solicitation for the purchase or sale of any security, financial instrument, or strategy. Any opinions expressed herein are given in good faith, are subject to change without notice, and are only correct as of the stated date of their issue.

This publication is designed to provide general information about ideas and strategies. It is for discussion purposes only, since the availability and effectiveness of any strategy are dependent upon each individual’s facts and circumstances. Always consult with your independent attorney, tax advisor, investment manager and insurance agent for final recommendations and before changing or implementing any financial strategy.

Nonfinancial assets, such as closely-held businesses, real estate, oil, gas and mineral properties, and timber, farm and ranch land, are complex in nature and involve risks including total loss of value. Special risk considerations include natural events (for example, earthquakes or fires), complex tax considerations, and lack of liquidity. Nonfinancial assets are not suitable for all investors.

Diversification does not ensure a profit or protect against loss in declining markets.

U.S. Trust operates through Bank of America, N.A., and other subsidiaries of Bank of America Corporation. Bank of America, N.A. and U.S. Trust Company of Delaware (collectively the “Bank”) do not serve in a fiduciary capacity with respect to all products or services. Fiduciary standards or fiduciary duties do not apply, for example, when the Bank is offering or providing credit solutions, banking, custody or brokerage products/services or referrals to other affiliates of the Bank.

Bank of America, N.A., Member FDIC.

© 2013 Bank of America Corporation. All rights reserved.