PHOTO: GREGG HILLYER

Red Hot Leases

Cash rent is the agreement of choice as landowners demand higher rates. But relationships can still play a part in who farms the land.

BY KURT LAWTON

A highly charged marketplace is making crop shares a relic of the past. In Iowa, upward of 70% of leases are now cash rents. But trying to quantify exact amounts growers are paying (or landowners are receiving) is like asking for the keys to Fort Knox.

Every grower and landowner we talked to for this story would not divulge specific cash rents paid or charged, citing the competitive landscape for farmland.

"They want to know what others are paying, but they don't necessarily want others to know what they're paying," says Iowa State University ag economist William Edward, who heads up one of the few anonymous cash-rent surveys in the Midwest.

One factor driving this "mum's the word" competitive approach is the climbing rents—and the huge range of rents being paid.

"Our 2008 Iowa survey [960 respondents] showed that, on average, rental rates climbed 15 to 20%, which is the biggest one-year increase since we began asking in 1994," Edwards says. "And that's on top of the second biggest increase of 9 to 10% last year."

HUGE RENTAL RANGE. The chart (see page B-3) shows cash-rent averages in Iowa over the past five years. Other Midwestern states have experienced similar increases. But the chart only shows a portion of the story.

High-quality land in 2008 rented for an average of $210 per acre in Iowa, with 30 counties reporting at least one rate of more than $300 (highest was $375). More than 45 counties (45% of Iowa) reported at least one rental rate of $275 and higher. And the range within a county for high-quality land can vary by more than $150 per acre.

Edwards says this wide range reflects the uncertainty over grain prices, "which is really what's driving rent these days. But the other aspect," he continues, "where growers are paying lower rates is often due to long-term relationships where perhaps landlords don't see the need to tie rent as closely to current grain prices.

"That's because they get other benefits beyond the money," Edwards says.

YOUNG FARMER TOUTS RELATIONSHIPS. With prime central Iowa farmland rents screaming upward last winter toward $300 an acre, you'd think young farmers would run fast in the other direction. But not Dave and Fonda Nelson.

Dave's past experience working for

Monsanto selling Roundup against generic competitors gave him valuable insight into differentiation marketing. He parlayed that into reasonable rents as the Nelsons began their second year of farming in 2008.

"There wasn't enough room in my parents' Fort Dodge-area operation, so we implemented a plan to start acquiring our own acres. And I wasn't just going to pay top cash rent to acquire land because that doesn't set the stage for a sustainable and profitable lease arrangement for both tenant and landowner," Dave says. "The traits I want to share with landowners are open communications, trust, business relationships, mutual long-term goals and increased net income for both parties."

THE HUMAN APPROACH. So the Nelsons crafted a resumé brochure in 2006, then implemented their leasing strategy—which had nothing to do with flexing prices or yields. It involved selling their personal dreams and farming/business practices.

Over the past two years, the Nelsons have shared their business approach and brochure with farm managers, ag loan officers, older farmers nearing retirement, seed dealers, elevator managers and a few larger landowners.

The couple's efforts are just beginning to pay off. "We had a substantial number of acres come to us—landowners looking for new tenants. Granted, most of these landowners decided to pursue higher cash rents. Thankfully, we were fortunate to end up with about 10% of those acres, plus some encouraging signs for the future," Nelson says.

HOT MIDWEST COMPETITION. Jim Farrell, president and CEO of Farmers National Company that manages more than 3,700 farms (1.3 million acres) in 20 states, has been surprised at the growth of cash rent and the number of growers vying to get more land.

Iowa farmers Dave and Fonda Nelson, with children Tyson and Morgan, seek a business relationship that benefits both parties when negotiating leases.

PHOTO: KURT LAWTON

"There has been a big increase in cash-rent leases in the past eight to 10 years. We've seen a huge increase in Iowa, and cash rents are spreading west into Nebraska and east into Illinois, Indiana and Ohio," Farrell says.

Fortunately for Southern farmers, they are not facing the same level of land competition. "We have much lower land turnover and more long-term relationships between farmers and landowners here in the Mid-South," says Bill Shannon, farm manager for Farmers National in Jonesboro, Ark.

"Crop-share leases [some of which have shared input costs] still comprise the bulk of agreements because the landowner has better income potential, but with less risk to the farmer," continues Shannon.

"Due to our more common drought risks and crops such as cotton and rice, which have higher input costs compared to the Midwest crops, growers will not pay high cash rents with the risk of not making a crop.

"Whereas $175 per acre would be considered a high cash rent, landowners may receive more than $300 per acre with excellent yields under a crop-share lease," adds Shannon.

But with prime Midwest land prices blowing past $5,000 and $6,000 per acre, most landowners realize they deserve higher rent to help pay for higher land taxes. However, growers we talked to for this story were quick to point out the added risks they face in skyrocketing fertilizer, seed, fuel costs and the inability to lock in future crop sales.

Still, most said they are looking for more land to lease and are willing to pay higher cash rents to get it.

GREAT RISK, HIGHER PROFIT. What is truly fueling this land jump—like in the late 1970s—is gross revenue, moving faster than a speeding bullet (sorry, Superman). "This revenue has totally changed the tenant-landlord dynamics in corn, soybean and wheat country," says ag banker Kent Thiesse, who works for MinnStar Bank in Lake Crystal, Minn.

"For example, in 2006, given 170-bushel corn, growers were looking at $400 to $500 per acre with government payments. Now, they're probably looking at $800 to $1,000 per acre in gross revenue," he says.

"But for landowners who no longer live in the farm community where they own the land, they often don't understand that the input costs for fertilizer, fuel and seed have gone up dramatically. Those costs have moved the break-even price bar for corn up to around $3.25 per bushel or more, compared to about $2 a bushel in 2006," says Thiesse.

LANDOWNERS ARE HUMAN TOO. Fortunately, many retired farmer landowners still remember the late 1970s and the subsequent land value crash by the mid-1980s that forced some friends and neighbors to give up the life they loved.

"I work with a lot of landowners who are cautious about getting too carried away with raising land rental rates too much; they know the costs are going up for the producer and there could be a big adjustment coming," Thiesse says.

"There are still some very good long-term relationships between tenants and landowners who don't want to break up a relationship just to grab quick money that someone may be offering for one year."

FLEXIBLE LAND DEALS. For all the talk about flexible land leases (base rent with flexible bonus fee tied to price and/or yield), the adoption of these less-than-simplistic land deals has yet to gain much momentum.

The initial challenge is to decide how to structure the bonus portion. If growers/landowners tie the flex bonus to actual yields or actual prices received—instead of county yields or local elevator prices—then the FSA will consider this a crop-share lease instead of cash rent, and you split government payments.

Luc Valentin, Purdue University ag economist, has worked with many farmers and landlords this past year to analyze leasing arrangements.

"In today's risky and more volatile environment, it should make flexible leases more popular because both sides can find mutual benefit. But we also recognize that some landowners and some larger farmers (with 30 to 40 landowners or more) value the simplicity of cash rent," Valentin says.

COMMUNICATION. "The best lease deals can occur when both sides figure out what is important for the other party and don't keep things hidden or only provide information when asked. If you don't communicate openly, you risk losing trust," he says.

Just ask the Nelsons about their eight-page color newsletter they send to landowners (current and prospects) several times a year.

"We believe in open communications, which leads to no surprises with our landlords. Marketing our operation is just as important as marketing our crop, and both areas strengthen our farm long term," Dave says.

Leasing **resources**

Purdue Leasing Resources
www.agecon.purdue.edu/extension/pubs/farmland_values_resources.asp

Ag Decision Maker—Leasing (Iowa State University)
www.extension.iastate.edu/agdm/

Farm Leasing e-School
www.extension.iastate.edu/ames/fla.htm