Farm Credit Canada

Canada

January/February 2006

AgriSuccess JOURNAL

Farmland: buy or rent?

How you answer this question depends on a number of factors – some of which you may not have considered.

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AgriSuccess JOURNAL

January/February 2006

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On the cover

Tom Halpenny (right) of Triticum Management Consulting has worked with hundreds of producers to develop business plans for grain, cattle, feeder hog and other operations.

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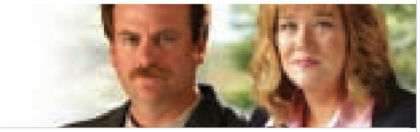
Letter from the editors



FROM KEVIN HURSH AND ALLISON FINNAMORE

Whether on beef cattle, hogs, dairy heifers, potatoes, canola, corn or wheat, market analysis is a mainstay of agricultural information. Supply and demand tables are constructed and carryover stocks are estimated. From this, analysts try to establish price trends.

Producers are eager to know how the market looks and they're also interested in marketing strategies including ways to capture profitable prices when they appear.

While critical to most farm operations, there is less analysis done on farmland prices. Even if you aren't in the market to buy land, the value is usually a major portion of a farm's net worth. If you are expansion-minded, what does the future hold for land prices and is it better to buy land or rent it?

These important questions are regularly discussed by producers across the country and they form the theme for this edition of AgriSuccess Journal. We hope you find these articles (and all the others) useful and interesting. We appreciate any comments you may have. You can reach us by e-mailing to info@Agrisuccess.ca or by calling 1-888-332-3301.

Kevin Hursh   Allison Finnamore

AgriSuccess JOURNAL

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Kevin Hursh is a consulting agrologist, journalist and broadcaster based in Saskatoon, Sask. He also takes an active role in the management and operation of a grain farm near Cabri, Sask.

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Allison Finnamore is a freelance agriculture journalist from Moncton, N.B. She's been writing about the region's agricultural issues for 15 years and is past president of the Canadian Farm Writers' Federation.

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The editors and journalists who contribute to AgriSuccess Journal attempt to provide accurate and useful information and analysis. However, the editors and FCC/AgriSuccess cannot and do not guarantee the accuracy of the information contained in this journal and the editors and FCC/AgriSuccess assume no responsibility for any actions or decisions taken by any reader of this journal based on the information provided.

The Canadian dollar effect

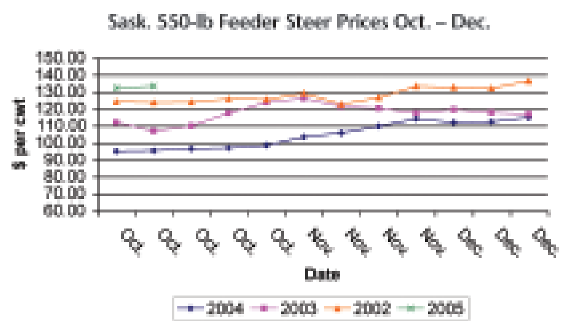
BY ALLISON FINNAMORE

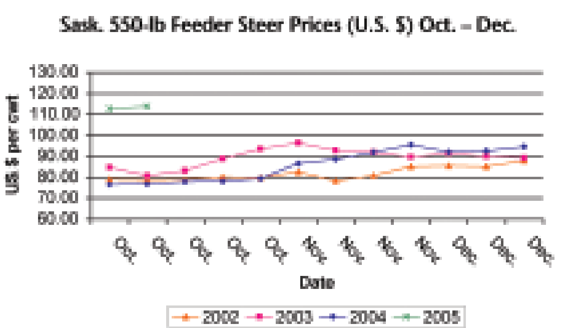
The rising Canadian dollar is having a big impact on the value of exports. In the fourth quarter of 2005, the dollar was around 85 cents US. Back in 2002, it was in the low 60s.

Sandy Russell, a beef economist with Saskatchewan Agriculture, uses information from Canfax to develop graphs below vividly illustrate the impact.

The top graph shows that 550-pound feeder steer prices started this fall's calf run at levels above those in past years. The second graph uses the same market prices, but it is adjusted into U.S. dollars based on the monthly average exchange rate.

When the higher Canadian dollar is taken into account, this year's feeder price, when expressed in U.S. dollars, is dramatically above previous years.





Web tips

COMPILED BY D. LARRAINE ANDREWS

Here are a few websites designed to help save you some time and money:

http://strategis.ic.gc.ca/epic/internet/insof-sdf.nsf/en/Home. The Buy vs. Lease calculator compares the costs involved in buying vs. leasing assets. The calculators are listed in the left-hand menu.

www.hrdc.gc.ca Search for "Canadian Retirement Income Calculator" to calculate a forecast of annual pre-tax retirement income.

www.bankofcanada.ca/en/rates/exchange.html Get historical exchange rates.

Aligning potato supply and demand

BY ALLISON FINNAMORE

North American potato production dropped in 2005 as producers made a bid to match supply and demand.

Canadian crop production dropped about 24,000 acres, or 6.5 million hundred weight, in 2005. In Prince Edward Island, producers agreed to reduce the typical 100,000-acre production by 9,600 acres. The U.S. potato crop dropped 11 per cent in 2005, an estimated 15.6 hundred weight of potatoes.

The American group, United Potato Growers Co-operative, is leading the move to increase producer profits by decreasing the potato market glut. The group met twice last year with producer groups from Prince Edward Island, New Brunswick, Quebec, Ontario, Manitoba, Alberta and British Columbia in an effort to get the entire North American potato industry working to reduce production. A steering committee has been formed in Canada to work out details of a partnership with the U.S. group.

Moving to opportunity

BY KEVIN HURSH

It's a difficult decision to sell your farm in order to buy a farm in another country. Yet, there's a continuing immigration of producers into Canada.

From the Netherlands, England, Scotland, Ireland and many other nations, producers come to Canada seeking opportunity. They aren't coming in droves like in the early 1900s when people flocked to Western Canada for the promise of free land, but the numbers are still significant.

> There aren't many Canadian farmers selling out to go farming in some other country.

In most western European nations, land prices are astronomical by Canadian standards. Prices of $5,000 to $10,000 an acre are common. On top of that, there are often restrictions on how the land can be used.

Despite extensive agricultural and rural support programs in Europe, it's difficult to afford the purchase of land. In many cases, it's difficult to expand a farm at any cost.

Farmland prices vary widely across the different regions of Canada, but for Europeans, our land is usually viewed as a bargain. In fact, European producers are often in disbelief when they hear the price of land in this country.

Even with less expensive land, creating a viable farm is far from a sure thing, but many recent immigrants have done very well in Canada. Some start out in one area of the country and then as they learn more about the different regions, they move again.

There aren't many Canadian producers selling out to go farming in some other country, but maybe there's something to be learned from those who pull up roots to move here. Sentimentality is natural and understandable, but it doesn't substitute for economics.

Canadian land prices are higher in areas pressured by urbanization and in areas where higher value agricultural production is possible. These areas can also be good for raising beef cattle and growing grain, but it may be tough to afford land for that type of production in high-priced regions.

Conversely, u-pick operations and agri-tourism ventures need people. Operating on less expensive land may not compensate for the lack of nearby population. Other types of production, such as tomatoes for processing, must be done in reasonable proximity to the processor.

Most farms are family ventures passed down over generations. It's home, there's roots and rarely is there any consideration given to moving to a different region of the province or the country.

In some cases though, homegrown Canadian producers might find relocation enhances their opportunities. It's like immigrating without changing your country.

Farmland: buy *or* rent

BY LORNE McCLINTON

Location, location, location, is real estate's golden rule and few farms in Canada have a location better than Jim Herder's at Sylvan Lake, Alberta. How good is it? Herder says a nearby quarter section (160 acres), with lakefront, recently sold for $3.8 million ($23,750/acre). The new owners got a bargain. After subdivision, the same land could easily fetch $16 million in a year or two. Sylvan Lake is a great place to buy farmland, as long as you don't intend to farm.

"The big questions is how much more are you willing to pay?"

"Land values are not determined by agriculture in our area," Herder says. "We purchased a quarter about four years ago. It will take virtually all the profit that we make off of all the land we own for the next 10 years just to pay for that one quarter. It's been a good investment. Land prices are still going up in this area and that's virtually the only reason why we do buy."

"Whether it's better to buy versus rent land depends on the situation of the farmer," says Brian Perillat, with Alberta Agriculture in Edmonton. For example, even though buying land may be a good real estate investment at Sylvan Lake, Herder is reluctant to take on more debt to buy land since the outbreak of BSE. For now he feels it makes more sense to rent than to buy. More than 75 per cent of his land base is rented.

"Before renting or buying land, producers have to consider the profitability, affordability and desirability of expanding their farm business," Perillat says. "If it is profitable, producers then have to decide if it is more profitable to own the land or rent it. Affordability relates

to cash flow – servicing debt and paying taxes in a purchase situation, or paying the rent fees in a rental situation. In high land value areas, affordability, not profitability, often becomes the deciding factor in a buy versus rent decision."

Perillat says desirability is making sure you are still moving towards your business goals, which would be expanding versus trying other ventures.

"Theoretically you should be willing to pay more to buy than to rent, the big question is how much more are you willing to pay?" says Laurie Baker with McGill's Macdonald College in St. Anne de Bellevue, Quebec. "When you purchase land, you are also purchasing the right to sell that land, which may or may not make some capital gain. In a rental market, you are only looking at the net revenue generated from the land after rental payments and operating costs."

Herder turns down land every year because "any land I rent has to be profitable. We have a feedlot and have to spread manure so land that's close to us has more value. If it's only a mile away, the rent is basically free because the reduced trucking costs more than pay for the rent of the land."

Herder says one disadvantage to renting is his land base isn't stable. While he expanded by 600 acres in 2005, he expects to lose 300 acres in 2006. This means it is risky to purchase machinery just to take on more rented land. Before taking on any new land, he recommends that you first determine that you have the time, labour and equipment to handle it.

There are no hard and fast rules when making a decison to rent or buy. Ultimately, it all boils down to determining what's right for every farm's unique circumstances.

Agriculture is lifelong learning

The learning never ends, especially if you are in agriculture, an industry brimming with innovation and advancement. It's difficult to grow your business or your understanding of agriculture, without being open to the idea of lifelong learning.

"We help Canadian producers improve their management skills and stay on top of agriculture," says Lyndon Carlson, FCC Vice-President, Market and Product Development. "We believe skills development and business management training are keys to greater success. For us, it's as important as offering the right financing, insurance, software and easy access to agriculture news."

Farm Credit Canada (FCC) offers workshops for human resources management, succession planning, financial management and goal setting. A multi-day course on farm management principles is available to help take your business to the next level.

Some of Canada's leading agriculture experts are instructors for the FCC Advanced Farm Manager course, focusing on an agricultural environment review, strategic planning, human resource management and succession planning. It also covers financial accounting, price risk management, strategic alliances and environmental policies.

"Successful business owners are those who seek out learning opportunities," says Michelle Painchaud, FCC AgriSuccess instructor. "I often hear business owners say they're too busy to take classes or attend information sessions. Ongoing learning is a must for every business owner. If you want to grow and want your business to grow, you have to keep learning."

Workshops are now being held across Canada. To register for a workshop or Advanced Farm Manager, call FCC at 1-888-332-3301 or sign up under the Learning Centre on www.fcc-fac.ca.

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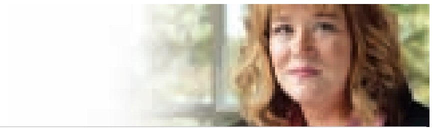
Promoting staple foods



BY ALLISON FINNAMORE

In the depths of winter, many Canadians turn to the kitchen to seek soothing comforts – piping hot potatoes, fluffy scrambled eggs, wholesome good bread and icy milk – soul food for many across the nation.

Turn on the television or flip through a Canadian magazine and you're likely to find advertisements for these staple foods. Egg and milk promotion are common, and last fall, potato producer organizations from Prince Edward Island, New Brunswick, Manitoba and Alberta teamed with McCain Foods Canada to promote potato nutrition in the Potato Facts campaign. At the same time, the Canadian Wheat Board, Canadian Pasta Manufacturers Association and the Baking Association of Canada joined together for a campaign called "Grains, They're Essential," promoting the nutrition of Canadian grains.

Most Canadians are also familiar with the "Get Cracking" egg slogan.

To some, it may not make sense to promote the basic foods that make up the foundation of so many Canadian diets. Yet, just because the foods are there, doesn't mean their consumption remains steady. The latest numbers from Statistics Canada indicate that the 2004 per capita consumption of fresh vegetables dropped for the third consecutive year, dipping to its lowest level since 1992. On average, Canadians consumed 74.8 kilograms (that's 164.8 pounds) of fresh vegetables in 2004 – a decrease from the 75.7 kilograms (or 166.5 pounds) consumed in 2003.

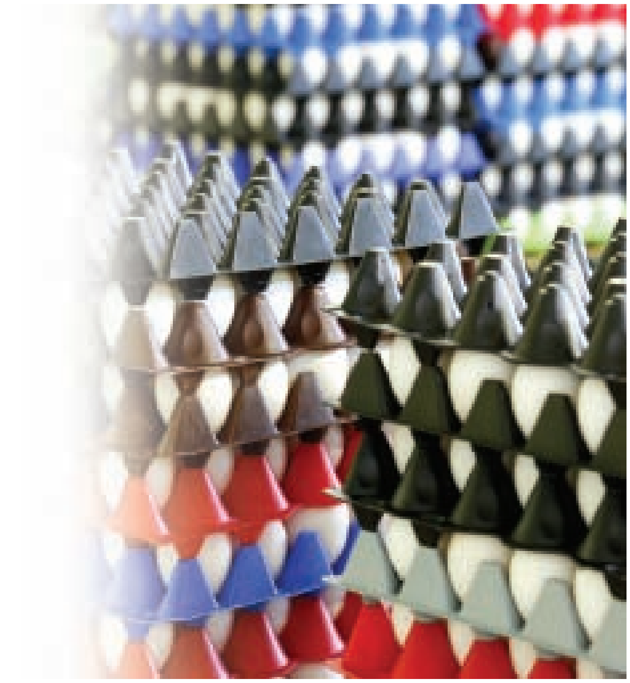
Potatoes, many of them eaten as french fries or chips, account for half of the decline in vegetable consumption, a downward trend over the last three years. Still, other basic vegetables like onions, lettuce and carrots have also experienced declining consumption.

Dr. John Cranfield is associate professor in the Department of Agricultural Economics and Business at the University of Guelph. He says advertising campaigns like the ones currently underway in Canada tend to target these kinds of issues and encourage consumers to increase consumption.

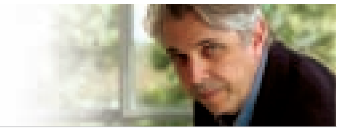
"Generic advertising is intended to increase demand for these products, which typically works to increase sales and the price received by producers," Cranfield says, adding campaigns can top $10 million.

The campaigns tend to work. Most Canadians are familiar with the various fluid milk campaigns from across the country, and are also familiar with the national "Get Cracking" egg slogan. Still, Cranfield stresses that it's only possible to assess the effectiveness of the campaign after it has ended. "It is very difficult to crystal ball how successful any particular campaign might be."

Despite foods like grains, potatoes, milk and eggs creating the foundation for many Canadian diets, there's still room to increase these markets and improve sales. Sometimes, perhaps caught up in the latest diet trend, we may forget that a varied diet of wholesome food grown by Canadian producers may in fact be the true key to overall health.



Measuring cow burps



BY OWEN ROBERTS

Cud-chewing cows have taken a public whipping for their alleged contributions to global warming. But it's a bum rap, because the farm sector is such a bit player when it comes to greenhouse gas output – it accounts for just eight per cent of Canada's overall total. Consider the energy sector (which includes vehicle exhaust) at 81 per cent, and you unmask the real culprit. Says Dr. James France, of the Centre for Nutritional Modelling in Animal Production Systems, University of Guelph: "When it comes to greenhouse gas, blame cars, not cows."

"When it comes to greenhouse gas, blame cars, not cows."

That said, livestock do indeed contribute almost half of agriculture's total greenhouse gas complement. So scientists such as France's colleague Dr. Brian McBride and research associate Dr. Nicholas Odongo, at Guelph's Department of Animal and Poultry Science, are doing their bit to help agriculture lower its output. As part of the national Greenhouse Gas Mitigation Program, which develops soil, nutrient and livestock practices to reduce greenhouse gas emissions, they're identifying environmentally friendly feeding programs they believe could cut contributions by five to 10 per cent – maybe even as high as 20 per cent – without affecting production efficiency.

Those are significant figures. But there are several "knows" in this research. For example, they already know some feeds promote production. And they also know some feeds (high-fibre diets, especially) give cows more gas.

But the relationship between feed efficiency and ruminant gas production is not well known…in part, because it's not easy to document. Feeding them and weighing them is one thing. But how do you measure their gas output?

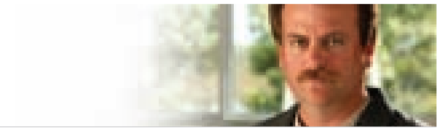
It could be a messy affair if that answer centred around emissions coming from the tail end. But mercifully, it doesn't. For example, most methane emissions from cows – 85 per cent, in fact – come from feed fermentation in the rumen. The process creates gas, which enters the atmosphere when the cows burp.

And that's the rub. Obtaining analytic breath samples from cows is not a common, well-established scientific procedure.

So McBride and Odongo invented what they're calling a "head hood" – a custom-built, sealed box that fits over a cow's head, and can be worn inside the stall. Each hood includes a window so the animals can see their neighbours, and a vacuum system to collect the animal's expired air. The researchers gather samples, analyse the expired air for carbon dioxide, oxygen and methane, and relate their findings back to the animal's feed. Ultimately, they'll compare the feed type to milk production.

Can they ever wipe out cow-generated greenhouse gas? Not likely, says McBride. But he thinks they can make a meaningful dent, without sacrificing the bottom line. And that should keep environmentalists and farmers happy.

Know your numbers



BY KEVIN HURSH

Federal/provincial support is available through the Renewal Pillar of the Agriculture Policy Framework to help producers assess their financial situation and develop an action plan for their farm business.

Under the Canadian Farm Business Advisory Service, a consultant works directly with an individual producer. Up to three days are spent on a financial assessment, with another two days to assess options for increasing farm profitability.

"Planning for the future starts with a thorough understanding of your current situation."

For services valued at $2,000, a producer is typically required to pay only $100.

Each province has a list of consultants registered under the program. For Saskatchewan and Alberta, one of the consultants on the list is Tom Halpenny of Triticum Management Consulting in Saskatoon.

Over the years, Halpenny has worked with hundreds of producers developing business plans for grain, cattle, feeder hog, greenhouse and field vegetable production and a few dairy operations.

According to Halpenny, no matter the type of enterprise, one of the most important aspects of business planning is to have an accurate handle on the costs of production.

For grain producers, he recommends projections before seeding and after harvest and then again at the end of the fiscal year using updated numbers each time. By knowing the cash costs and the non-cash costs per acre, producers know the crop prices and yields they need to break even and hopefully turn a profit.

"It's a big benefit for marketing as well as budgeting," notes Halpenny.

The same principle applies to other types of operations. For beef, the cost per pound of weaned calf can be calculated. In dairy operations, it can be the cost per kilogram of milk produced.

Farms with multiple types of production need to analyse each as a separate enterprise. If you use the same tractor for swathing canola and feeding cattle, you have to apportion the costs between enterprises.

Halpenny also works with the family to estimate living expenses. This can also be added to the cost structure.

For many producers, the CAIS (Canadian Agricultural Income Stabilization) program is the fall-back position in a year when returns drop below the reference margin established from previous years.

Halpenny likes to calculate the price and production sensitivity for CAIS. In others words, how much would price and/or production have to drop before the producer might be in a claim position. This is especially important in difficult years and if the farm operation may be structuring up or down (expanding or contracting).

"Producers can view their operation in a whole new light once they have an accurate picture of their costs per unit of production," explains Halpenny. "Planning for the future starts with a thorough understanding of your current situation."

For more information on the Canadian Farm Business Advisory Service, go to the federal agriculture department's website at www.agr.gc.ca and click on Renewal.

Predicting *farmland* values

BY KEVIN HURSH

Decisions related to the buying and selling of farmland would be a lot easier if we could predict future values. If history is any indicator, land values trend upwards over the long-term, but there are also downward corrections.

Statistics Canada has information on the average value of farmland and buildings for each province dating back to the 1920s.

Farm income levels have not been good in recent years, but farmland values overall have not retreated.

The decade of the 1970s saw the most rapid escalation of farmland values the country has ever seen. From 1971 to 1980, the average value across the nation went from $100 an acre to $547. The magnitude of the increase was similar in every province.

Values peaked in the early '80s and then started to retreat. Those were times of very high interest rates and many producers were highly leveraged.

The farmland value slide was over by the mid-'80s in the Maritime provinces. For B.C., Ontario and Quebec, the bottom of the market came in about 1987. For the Prairies, the slide in values continued into the early '90s.

Since 1995, with only a few exceptions, farmland values have risen year over year in each province. However, the magnitude of the increase has varied widely.

Farm income levels have not been good in recent years, but farmland values overall have not retreated.

Bill Brown, an agricultural economist at the University of Saskatchewan, believes the returns enjoyed by some large, more progressive operations may be substantially higher than the average. He thinks these types of operations often influence farmland values in a local area.

The type of farm also makes a big difference. "In parts of the country where there's more stability in farm income from the supply managed sectors of agriculture, that tends to be capitalized back into farmland values," observes Brown.

Al Mussell of the George Morris Centre in Guelph says that in some parts of the country, agriculture drives farmland values, while in other regions, non-agricultural factors are the main drivers – everything from urbanization to surface rights leases from oil and gas companies.

"It's also astonishing how much off-farm income is used to purchase farmland," notes Mussell.

As proven by the '80s, farmland values do not always increase. It's also possible for values to go different directions in different regions due to different influencing factors.

Value per acre of farmland and buildings – Statistics Canada

	1995	2004	% Change
Nfld.	1,243	1,455	17
P.E.I.	1,545	1,882	22
N.S.	896	1,182	32
N.B.	754	1,161	54
Que.	1,114	2,022	81
Ont.	2,188	3,337	52
Man.	413	554	34
Sask.	299	350	17
Alta.	515	811	57
B.C.	1,767	2,266	28
Canada	634	927	46

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