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ECONOMICS COMMENTATOR

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SOUTH DAKOTA AGRICULTURAL LAND VALUES AND CASH RENTAL RATES, 2006



by
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We wish to thank the individuals who participated in the 2006 South Dakota Farm Real Estate Market Survey. Without their responses this report would not be possible. Special thanks to: Don Won Lee for data input and conducting the survey; Janet Wilson for maintaining the mailing list; and Barb Dininger for various survey tasks.

South Dakota's agricultural land values increased 14.4% this past year and have doubled since 2000. The average value of agricultural land (as of February, 2006) varies from \$253 per acre in the northwest region to \$1646 per acre in the east central region. These are key findings from the 2006 South Dakota Farm Real Estate Market Survey reports completed by 222 agricultural lenders, Farm Service Agency officials, rural appraisers, assessors, realtors, professional farm managers, and Extension agricultural educators.

This is the sixteenth annual SDSU survey designed to estimate agricultural land values and cash rental rates by type of land in different regions of the State. Summaries of prior survey results were reported in earlier *Economics Commentator* issues.

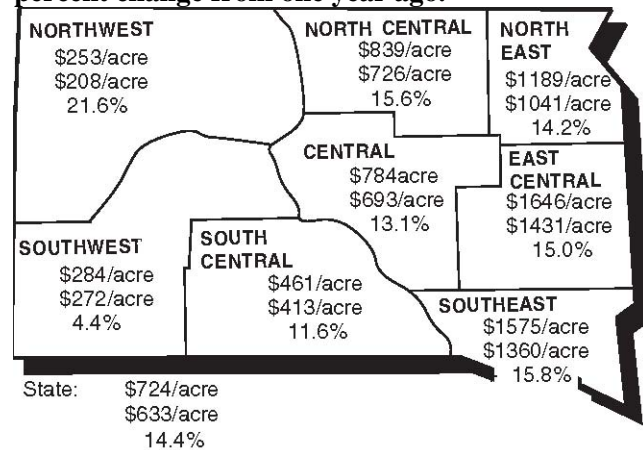
The information in this newsletter provides an overview of agricultural land values and cash rental rates across South Dakota. We caution the reader to use this information as a general reference, and to rely on local sources for more specific details.

Respondents provided county land value and cash rental rate information by agricultural land use. Responses, grouped by region with average values for all classes of land, are provided in Figure 1. Separate estimates of land value and cash rental rate information for nonirrigated cropland, irrigated land, hayland, rangeland, and tame pasture are provided in Figures 2-4.

Average Land Value Summary

As of February, 2006, the estimated South Dakota all agricultural land value average was \$724 per acre, a 14.4% increase in value from 2005 (Figure 1). The increase of \$91 per acre is the second highest annual dollar per acre increase during the 16 year history of this survey. Overall, agricultural land values in South Dakota have more than doubled since 2000 and tripled since 1993.

Figure 1. Average value of South Dakota agricultural land, February 1, 2006 and 2005, and percent change from one year ago.



Regional and statewide average values of agricultural land are the weighted averages of dollar value per acre and percent change by proportion of acres of each nonirrigated land use by region.

Top: Average per-acre value—February 1, 2006
Middle: Average per-acre value—February 1, 2005
Bottom: Annual percent change in per-acre land value

Source: 2006 South Dakota Farm Real Estate Market Survey, SDSU.

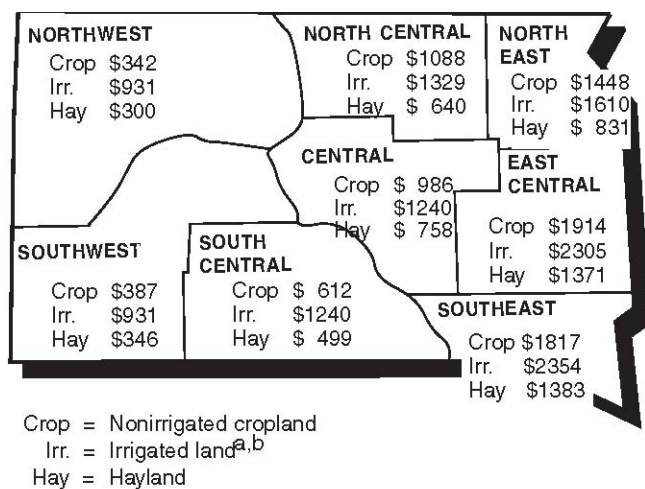
According to survey respondents, agricultural land values increased in all regions of South Dakota from 2005 to 2006. The largest rates of increases occurred in the northwest (21.6%) region, while the lowest were in the southwest region at only 4.4%. Land value increases were fairly close to the state average in the southeast (15.8%), north central (15.6%), east central (15.0%), north east (14.2%), and central 13.1%) regions.

Agricultural land values are highest in the east central region, followed by the southeast region. Cropland and hayland are the dominant land uses in these regions, which contain the most productive land in South Dakota. The lowest average land values are found in the northwest and southwest regions.

In each region, per acre values are highest for irrigated land, followed in descending order by nonirrigated cropland, hayland or tame pasture, and native rangeland (Figures 2 and 3). Within each region, there is substantial variation in per acre land values by use and land productivity.

Average nonirrigated cropland values range from \$1,914 per acre in the east central region to \$342 per acre in the northwest region of the state. Average rangeland values vary from \$1055 per acre in the east-central region to \$234 per acre in the northwest region of South Dakota.

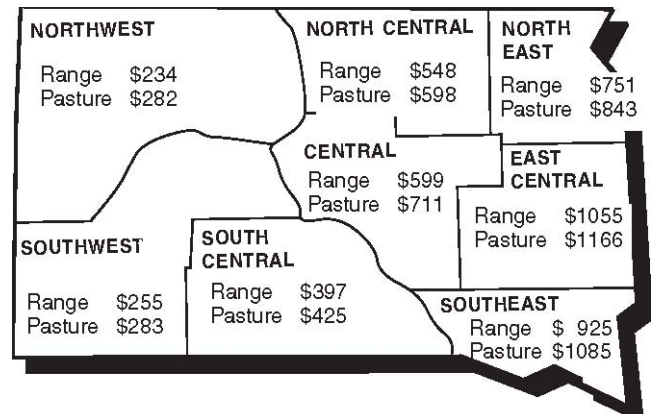
Figure 2. Average value of South Dakota cropland, irrigated land, and hayland, by region, February 2006, dollars per acre.



^a Irrigated land values shown for the northwest and southwest regions are based on the average value reported for gravity irrigated land in both western areas.
^b Irrigated land values shown for the central and south-central regions are based on the average value reported in both regions.

Source: 2006 South Dakota Farm Real Estate Market Survey, SDSU.

Figure 3. Average value of South Dakota rangeland and tame pasture, by region, February 2006, dollars per acre.

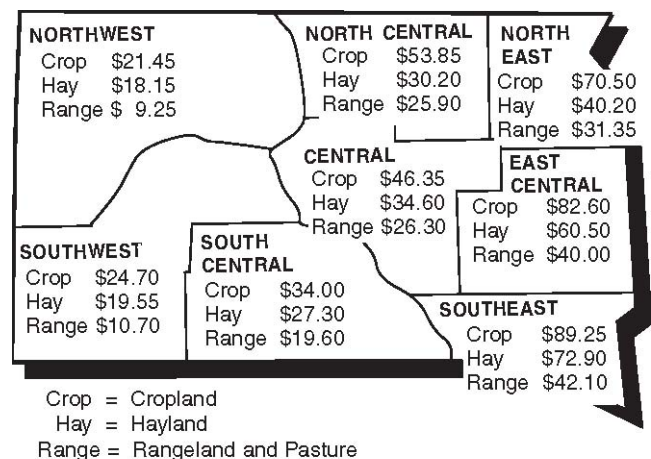


Source: 2006 South Dakota Farm Real Estate Market Survey, SDSU.

Average Cash Rental Rate Summary

The cash rental market provides important information on returns to agricultural land. Cash rental rates are quite variable among South Dakota regions. Within each region, the average annual cash rental rates are highest for cropland and lowest for pasture and rangeland. For each land use, cash rental rates are highest in the southeast region and lowest in the western regions (Figure 4).

Figure 4. Average cash rental rate of South Dakota nonirrigated cropland, hayland, and rangeland, by region, 2006, dollars per acre.



Source: 2006 South Dakota Farm Real Estate Market Survey, SDSU.

Average cash rental rates for nonirrigated cropland vary from \$89.25 per acre in southeastern South Dakota to \$21.45 per acre in the northwestern region. Average rangeland cash rental rates vary from

\$42.10 per acre in the southeastern region to \$9.25 per acre in the northwest region.

Cash rental rates per acre increased or remained stable for cropland, hayland, and rangeland in all regions of South Dakota, except in the northwest and southwest regions. Statewide, cash rental rates increased an average of \$2.05 per acre for cropland, \$2.35 per acre for hayland, and \$1.00 per acre for rangeland (table 1).

Table 1. 2005-2006 Change in Per Acre Cash Rent

	<u>cropland</u>	<u>hayland</u>	<u>rangeland</u>
Southeast	\$2.05	\$1.30	\$1.55
East Central	\$-0-	\$4.10	\$3.95
Northeast	\$4.80	\$1.50	\$1.55
North Central	\$4.45	\$1.30	\$1.30
Central	\$0.55	\$4.80	\$1.35
South Central	\$2.50	\$5.10	\$4.75
Southwest	-\$0.20	\$1.95	\$-0-
Northwest	-\$1.45	-\$0.80	-\$0.50
State	\$2.05	\$2.35	\$1.00

Rates of Return to Agricultural Land

The gross rent-to-value ratio (gross cash rent as a percent of reported land value) is a measure of **gross** rate of return to land, before deduction of property taxes and other landlord expenses. Gross rent-to-value ratios for 2006 averaged 5.2% for non-irrigated cropland and hayland, 4.3% for rangeland, and 4.7% for all-agricultural land. This is the first time in the 16 years of this survey that the average gross rates of return to all non-irrigated agricultural land is lower than 5%.

Respondents were asked to estimate **net** rates of return to agricultural land ownership in their locality, given current land values. Statewide, the estimated net rate of return to land averaged 3.9% for all agricultural land, 4.2% for non-irrigated cropland, 4.0% for hayland, and 3.8% for rangeland and pasture. This is the second consecutive year that average net rates of return for all-agricultural land were below 4%. Also, average net rates of return in 2006 are below 4.5% for each agricultural land use and for all regions of South Dakota.

The projected difference between gross and net rates of return to agricultural land ownership in 2006 is 0.8 percentage points for all-agricultural land and varies somewhat across regions and agricultural land use. Most of the difference between gross returns and net returns is caused by property tax levies.

Farmland investors and buyers are currently in market conditions where an increasing proportion of total returns are from expectations of capital appreciation

instead of current cash returns. This pattern of declining rates of cash return to land also occurs during the latter stages of land market price booms.

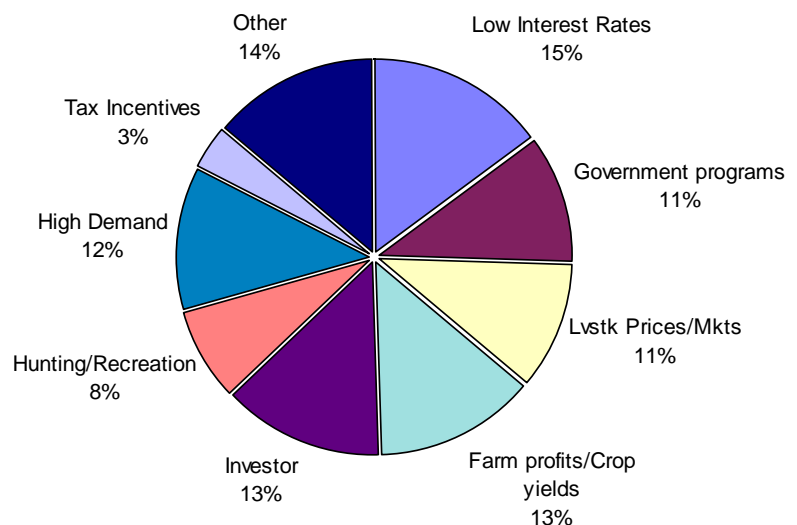
The longer-term trends in land values, cash rental rates and cash rates of return, are closely related to key economic factors including: (1) sharp declines in farm mortgage interest rates from early 2001 to late 2004; (2) federal farm program provisions of the 1996 and 2002 farm bills, especially the level of crop subsidies and removal of planting restrictions; and (3) general economic conditions of low inflation rates.

Ag Land Market Factors

Respondents listed major positive and negative factors affecting the farm real estate market in their localities. These factors help explain changes in the amount of farmland for sale, sale prices, and rental rates.

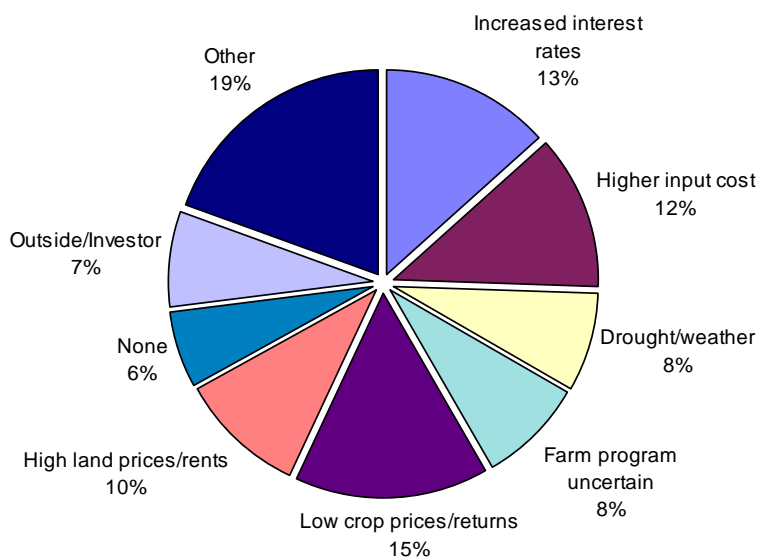
Among positive factors influencing the farm real estate market, low interest rates were identified most often by respondents (15%). Other positive factors were high crop yields/profits and investor interest (each 13%), high demand (12%), and government programs and livestock prices (each 11%), followed by hunting/recreation (8%) and tax incentives (3%).

Figure 5. Positive factors in the farm real estate market



Major negative factors in the farm real estate market include low crop prices/returns (15%), increased interest rates (13%), higher input costs (12%), and high land rents (10%). Drought/weather conditions and farm program incentives (each 8%) were also reported as negative factors, as well as outside investors (7%).

Figure 6. Negative factors in the farm real estate market



Respondents identified major reasons for buying and selling farmland. Farm land expansion and investment purposes were the most common responses for purchasing farmland, along with hunting/recreation. Retirement, estate settlement, and existing market conditions continue to be major reasons for selling farmland.

One half of respondents provided their land value forecast for next year. Eighty percent of these respondents expect land values to increase in the next 12 months, while most others expect no change. Similar to last year, the median forecast percentage change in land values is a 5% increase for each land use.

In summary, respondents remain optimistic about prospective farm/ranch land market conditions in the next year. However, more respondents, compared to 2005, express concern that the land market is becoming “overheated” as land values in the past 5 years have increased at twice the rate of cash rental rates.

Farmland values have increased much more rapidly than the rate of general price inflation from 1991 to 2006 in all regions and for all land uses in South Dakota. Cash rental rate increases continue to provide underlying support for an expected increase in land values. These basic economic factors attract continued interest in farmland purchases by investors and by farmers expanding their operations.

For more detailed information, a full copy of South Dakota Farmland Market Trends, 1991-2006, by Janssen and Pflueger is expected to be published in the coming weeks. Copies of that publication should be available from your County Extension Office.

NOTE: This special edition of the *Commentator* is being made available electronically on our website at: <http://econ.sdstate.edu/Research/Commentator/No475.pdf>. Our policy remains to provide electronic copies several weeks after our subscribers have received the newsletter.

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