Is This Boom Different: Repeat of the 70-80's?

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What is different than the 80's; Is a Bust Inevitable?

- Wealth Effect (buy land and other assets for gain rather than earnings) not as strong
- Leverage Effect (increased debt use based on appreciating asset values not as strong)

- Demand reduction likely not as dramatic.
  - Mandated biofuels demand
  - Asia/China demand unlikely to collapse
  - Dollar likely to not continue to rise
- Asset values not under as much pressure
  - Fewer forced sales from foreclosures
  - Most land purchases by farmers rather than investors

What Could Create a Bust?

- Unexpected demand reduction
- Reduced biofuels mandates
- Further aggressive bidding and rising values for farmland
- More concentrated debt than we realize
- Rising interest rates resulting in increasing value of the dollar, higher capitalization rates and higher costs and lower margins/incomes
- Increased Wealth Effect behavior (buying land for capital gains/inflation hedge)

- Increased "pseudo-debt" obligations (multi-year high fixed cash rent obligations)
- Imbalance in balance sheet (increased non-current assets not financed by non-current liabilities)
- Reduced working capital
- Liquidation of raised grain/livestock inventories which triggers deferred tax obligations
- Increased Leverage Effect behavior (borrowing based on appreciating asset values)

The Potential Credit Surprises

- Reduced liquidity/working capital
- Lower collateral/security values
- Debt structure challenges
- Triggering of deferred tax obligations
- Margin Compression
- Reduced income subsidy for expansion
- Counterparty risk

Why Will Capital Costs Eventually Be Higher?

- Higher cost of sourcing funds (risk premiums)
- Higher credit risk premiums
- Higher servicing/compliance costs
- Higher lender spread to rebuild loss reserves and reestablish profit margins
- Less competitive pressure on rates
- Higher transaction costs for borrower
- Higher potential rate of inflation
- Increased equity risk and inflation premiums

What to Watch:

Uncertainties Impacting Agriculture

What to Watch

1. The financial crises in Europe and the EU
2. The sluggishness of the recovery of the U.S. economy
3. The changing (now rising) value of the dollar
4. The unpredictable future growth of income in China and Asia more broadly

What to Watch

- 5. The recent and current weather induced short supplies of corn, beans and wheat
- 6. Current and future potential regulations on production systems (animal welfare, fertilizer/chemical use, etc.)
- 7. Increased acreage brought into production in response to higher prices (123 million additional acres in the world).
- 8. Uncertainty about changes in farm policy

What to Watch

- 9. The timing and amount of future changes in interest rates
- 10. Fluctuations in fertilizer, seed, chemical and energy prices
- 11. The prospects of a continued boom and potential bust in farm incomes and land values among others.
- 12. Counter party risks.

Closing Comments

- Long-term demand for food, feed, fiber and energy appears bullish
- The productivity challenge is significant but we have the technologies to meet the demand
- While long-term drivers are encouraging the path to the future will be volatile

Closing Comments

- Incomes generally adequate BUT
  - Operating risk has increased
  - Tools less effective/more expensive
    - Government programs
    - Futures options/crop insurance
    - Margin management

Closing Comments

- Assuming risk requires financial strength
  - Increase working capital
    - Reduce short-term debt
    - Fix interest rates
    - Negotiate an extended/larger line of credit
    - Slow growth rate
    - Maintain flexibility