

AN UNEXPECTED SOURCE OF FARM BUSINESS EDUCATION

Jay Lee Smith

Jay Lee Smith Farms, Owner- Manager, Summitville, Indiana USA

Abstract

I took my first international trip 48 years ago as a young farmer in the year 1974. My experience as a farmer has been that international travel has not been an expense for me. International travel has been a valuable investment. International agricultural farm travel with farmers can significantly improve one's inherent decision-making ability and thus actually be a profit enhancer to one's business. This case study related to fixed vs variable interest rate is one example. One should strongly consider avoiding short term variable interest rates. Changes in interest rates can have a huge impact on one's business profitability and survival.

Introduction

“A 1974 TRIP TO EUROPE SAVED OUR BACON”

Beginning a farming vocation in the 1970's after university typically involved “going home” to join a family farm, or working on a farm where you hoped for experience and advancement to establish your own operation, or working off the farm in an agricultural related field. The steps to financial management education did not include the unlikely experience of traveling “across the pond.”

Europe Farm Tour

Somehow, and I do not remember our reasoning, my wife Pamela and I at the age of 27 decided to purchase a two-week farm tour to Western Europe. We were in debt way over our heads and technically insolvent when we purchased this tour package with borrowed money. It was practically unheard of for anyone in our area to go to Europe. The WWII men

had been and that was practically all. So, for two kids to go across the big pond was seen by our elders as being way out there in crazy land and foolishly spending borrowed money.

We were with a tour group of American farmers and their wives to tour Austria, Italy, Germany, Lichtenstein, Netherlands, Switzerland and our tour started in Scotland and then on into England. I believe we were the youngest of the group by 30 years. Most of the farmers in our tour group were recently retired or were in the slowing down phase. Some had lost their first wife and were on this trip with their second wife. That is interesting to note.

The group seemed to look at us with a questioning gaze of what in the world are you kids doing on this trip? How can they afford it? Soon we had made friends with all and many had learned our story. In the second week three farmers individually took me aside and told me their story. It basically went like this: “My first wife and I milked cows together every day for 40 years and then she passed. Within six months of her passing I had sold the cows and eventually found myself a good lady and we fell in love and got married. Now we are both enjoying the fruit of the work of both myself and my first wife. Young man, you are doing right, work and live and share with your wife while you both can. Don’t wait until you are old and retired to travel.”

London England, 14% Interest

We were in London England on a tour bus traveling past lovely identical two-story white houses, one after another lining the street, and I asked the guide what one of those houses would cost. He told me and then I asked, “How can they ever pay for it?” He said that most will not. They get loans from insurance companies and pay the interest and pennies on the loan principal. When they die or move, the insurance companies will sell the house again and they or the estate will receive some equity. I asked, “What is the interest rate?” He said, “It is 14%.” My brain did a double take and I thought holy cow we are on the same railroad track waiting for the train to arrive.

Our variable interest rate was between 6 and 6.5% for our borrowed funds and the interest rate was adjustable and the loan could be called anytime the bank desired. We were in a very vulnerable and risky financial position.

Return to Farm

Soon after returning to our farm in Summitville, Indiana, we started investigating loan options from different potential lenders with a fixed rate for 20-25 year terms. Also, we got a professional appraiser to appraise all of our land and assets. At that time, we purchased an adjoining farm consisting of 90 acres. We borrowed every dollar that we could with a fixed interest rate of 7% amortized over a 20-year term. One half of the principal would be paid

with a balloon payment at the end of the 20 years for the remaining half. We borrowed all that we could using all of our assets as collateral and put two years principal and interest payments in a special investment bank in a high interest account with intentions to never touch it. Our reasoning was that if things got really difficult for us, we could still make two years payments from this account. To this day we have never touched these funds and have continued to build this emergency account.

Remember the title of this paper: 1974 European Farm Tour While in England Saved Our Bacon. In 1981 interest rates in the USA locally had reached 21.75% and farmers in our area were feeling financial pain. This economic debacle in USA Agriculture continued to reach its low in 1987 with land values at their lowest point.

Nearly all farmers were very concerned about their own financial health and with historically high interest rates were not interested in purchasing any land. We are located south of Chicago and the Great Lakes in what is called the Midwest, in the small village town of Summitville, Indiana. This is an area of essentially flat highly productive land with the predominant crops of Corn, Soybeans and Soft Red Winter Wheat.

Agriculture Recession of the 1980's

Some farm land in the 1977-1980 time frame in the Summitville area sold for \$2600. – \$2900.00 per acre. In May 1986, a neighbor's farm with some buildings and 4 small grain bins, The Prairie Grove Farm, sold for \$1,152.00 per acre (Smith May 1986). In 1987 at the bottom of the agricultural recession the Gossett Farm that had previously sold for \$2600.00 per acre sold for \$709.00 per acre (Smith May 1987). The severe fast decline of land prices in 7 years was followed by a slow recovery in land price. In March 1990 a nearby all tillable farm, The Milhollin Farm, sold for \$1059.00 per acre (Smith March 1990). By September 1992 a local all tillable land farm sold for \$1400.00 per acre and another sold with a livable house and barn for \$1421.00 per acre at a Sheriff's foreclosure sale (Smith September 2, 1992). This was the last foreclosure sale in our area due to the devastating historical high interest rate period. In year 2002 bare land in the area had recovered to the \$2600.00 per acre range with the local sale of, The Beeson Farm, consisting of 146.1 acres at a public auction sale, with a selling price of \$2635.00 per acre (Smith February 6, 2002).

The rise in land values has continued with some pauses and some declines; but has continued an upward spiral for 50 years averaging 6 % per year, from 1970 to 2020 (Schnitkey, September 21, 2021). Today, in our area the land price is rising very quickly with recent sales of good farmland selling in the \$12,000.00 to \$16,000.00 per acre range. On December 14, 2021, The Donna J. Clock Farm, 42.9 acres of bare land brought

\$13,000.00 per acre at public auction (Price-Leffler, 2021). \$13,000.00 per acre is equal to \$32,110.00 per hectare. One hectare is equal to 2.47 acres.

If we had not refinanced and locked in a 7% fixed interest rate with half of the principal amortized over 20 years with a 50% balloon payment at the end, we would have incurred the 21.75% interest rate and would have had severe financial difficulties perhaps ending in bankruptcy and foreclosure.

For example, we had a neighbor, M. J. that incurred severe financial difficulties and was forced to quit farming. M. J. incurred the 21.75% interest rate on some feeder cattle and when he sold the cattle his interest charge per head was \$56.00 (M. J. 2021). He had significant additional funds borrowed on a variable interest rate. Other farmers in the three-county area where we farm, entered into bankruptcy and were eventually in foreclosure.

We could not have paid 21.75% interest rate and survived. We would have defaulted and I would have returned to teaching Agriculture. With our fixed interest rate and with hogs being profitable to us, we did well during the very poor farm economy of the 1980's. Farmers that survived this agriculture depression now have land that is worth \$13,000.00 or more per acre. If the owner chose to rent this land, one could expect the land to rent in the \$300. - \$350.00 range per acre, if the land is properly drained with a pattern tile drainage system.

Conclusions

For the farmer, international agricultural travel, congresses, conferences and seminar participation has the potential to provide the farmer with business, agronomy and marketing information that has the potential to be very significant and of high value to his operation. The farmer's decision-making ability may be so improved that the international travel may not be an expense; but rather a profit enhancer.

One must thoroughly analyze loan interest rates and loan terms to determine what is best for the viability and survivability of one's business. With interest rates at historical lows the farmer should seriously consider locking in the historically low long-term rates for his farm operation.

References

- Leffler, M., 2021. Price-Leffler, Real Estate Auction Attendee Witness, Jay Smith.
M.J., 2021. Personal account of personal information, Jay Smith.

Schnitkey, G., K. Swanson, N. Paulson and C. Zulauf., 2021. "Debt Financing and Timing Farmland Purchases." *Farmdoc daily* (11):135 Department of Agricultural and Consumer Economics, University of Illinois at Urbana-Champaign.

Smith, J., 1986. Delaware County. Recorded Sale with Property Title.

Smith, J., 1987. Delaware County. Recorded Sale with Property Title.

Smith, J., 1990. Delaware County. Recorded Sale with Property Title.

Smith, J., 1992. Delaware County. Recorded Sale with Property Title.

Smith, J., 2002. Madison County. Recorded Sale with Property Title.