Corporate Investment in Agriculture

A report for

NUFFIELD AUSTRALIA FARMING SCHOLARS

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2011 Nuffield Scholar

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Foreword

Traditionally family farming has been the cornerstone of agriculture in Australia. Raising capital to expand and sustain family farming operations has become more challenging during the past decade due to ever-decreasing profit margins. During this time Australian farming has experienced some of the most severe climatic variability, volatile commodity prices and escalating input costs. Alternative business strategies must be continually examined and the ability to attract corporate capital will be an opportunity for a family farming operation to remain financially viable, aiding the potential for farm succession.

The high debt levels being carried by today's farmers can have a negative impact on personal welfare, local communities and suppress uptake of new technology and innovation. Models that provide positive outcomes for both the investor and farmer can reinvigorate the farming landscape and renew enthusiasm within the business and communities.

Historically corporate farms were large in scale or highly intensive operations using tiered management systems. The success of past models is being challenged with growing issues of management expertise and labour availability. There have been numerous examples of corporate investment previously in Australian agriculture that has failed due to fundamental flaws. This has resulted in many viewing corporate farms and investors with high levels of prejudice and negative associations with the concept. With these experiences it is evident that the future models are being more farmer-inclusive. To ensure the sustainability of these models participants share in profitability, longevity, integrity and risk.

There needs to be careful consideration about policy relating to foreign ownership laws and the impact this could have on land values and flow-on equity levels of existing farmers. The imposition of trade barriers on Australia could be a result of the tightening of foreign ownership laws.

Australia has very few barriers to corporate investment with low levels of government support. There is now a generation of farmers looking for an alternative for business growth and expansion and are unbiased toward sources of external investment.

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- The 2011 Nuffield Scholars that made it such a memorable year, particularly my Global Focus group.
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Abbreviations

ABARE – Australian Bureau of Agricultural Research Economics

APW – Australian Premium White

GRDC – The Grains Research and Development Corporation

Ha - hectare

OECD – The Organisation for Economic Cooperation Development

MIS – Managed Investment Schemes

WA – Western Australia

US – United States of America

EU – European Union

t - tonne

Vic – Victoria

NSW – New South Wales

SA – South Australia

NT – Northern Territory

UK – United Kingdom

NCREIF - National Council for Real Estate Fiduciaries

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Executive Summary

Farmland values have conservatively doubled throughout most Australian agricultural regions in the past 15 years. Conversely, farm productivity hasn't experienced the same rate of growth. Consequently farmers are looking for alternative options to remain viable and ensure long-term farm sustainability.

Corporate farming and foreign investment have always been a part of the Australian landscape. Recent global financial issues, along with growing concern over food security, are placing greater emphasis on agriculture as a secure investment.

The aim of my studies was to determine:

- which investment companies and countries are active in agricultural investment
- why Australia is an attractive country for investment
- barriers and restrictions on rural investment outside of Australia
- the influence of Government support on foreign and corporate investment
- evaluate the various investment models used globally
- investigate opportunities for Australian family farming businesses to form relationships with these corporate investors.

I travelled throughout Brazil, Mexico, France, Ireland, the United Kingdom, Central and Eastern Europe, Canada, United States, New Zealand and Australia. I spoke with farmers, University professors, consultants, researchers, fund managers, bankers, government agencies and politicians to gain a greater understanding of managing the challenge of accessing capital in a sustainable manner.

The key finding from my research is that Australian agriculture is a highly attractive location for corporate investment funds for a number of reasons, including political and economic stability; reliable, low risk returns and comparatively minimal restriction for land access. Government-backed sovereign wealth funds with concerns over their own food security see Australia as an opportunity.

The challenge for investors and agriculture in general is to develop and examine models that have "real" sustainability to all involved. There are future models emerging that will assist farmers manage production risk via co-investment. The historical ownership and operational structure of Australian farming is changing and farmers must be open minded with regard to the opportunities external capital can have on their business via corporate investment.

Introduction

At the completion of an Agricultural business Degree in 1994 I married and returned to the family farm which at that stage consisted of just over 2,000 ha. Over the ensuing 16 years the farm business was expanded through land purchases and leasing to grow to 14,800 ha, as well as the purchase of machinery and development of infrastructure to manage the scale of the enterprise. This expansion accommodated the return of three more brothers after completing trades and tertiary qualifications. This growth was achieved using traditional bank finance arrangements. Over this period of time land values, both for freehold purchase and leasing, rose significantly.

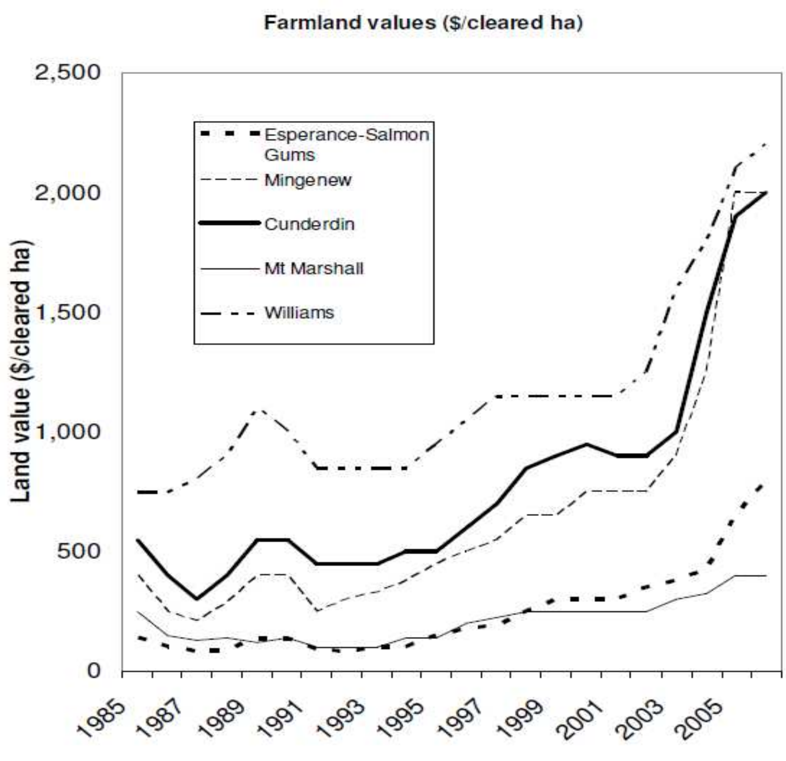


Figure 2: Land values in various shires in the broadacre region of Western Australia: 1985 to 2006 ($/cleared ha).

Source: Based on data supplied by Landgate

However, from 2008 onwards, the cost of our variable inputs, e.g. fertiliser, chemical, fuel and machinery, rose significantly in response to a large grain price spike. Although some of these direct costs declined slightly post-2009, so did the global wheat price to a point where, at the beginning of 2010, the forecast for

APW wheat net farm gate for harvest was $180 - $200/t. This price, combined with our average production per hectare would result in an operating loss.

Along with the huge volatility that is occurring with global grain pricing, Australian farmers have faced some of the most variable climate scenarios in the past decade.

So this is where, as an individual involved in a family farming business, I became concerned – what strategies do we undertake to move the business forward?

The key phrase I used within our faming business was that in all growing regions of Agriculture in WA the price of land had now exceeded its production capability. Thinking that this was a new phenomenon and explaining this to Bruce Sherrick, a Professor in Agricultural Economics at the University of Illinois, he directed me to a quote from Professor George Morrow, who had stated the same concern in the US back in 1896.

So this is not new to global Agriculture, but has impacted more directly in Australia, and even more so WA, in the past five years. Our risk profile has risen dramatically and our growth opportunities through traditional debt financing are being challenged. What alternatives does a young farmer coming home onto a family farm have when they have to deal with family farm succession, climate variability, rising input costs and volatile commodity markets in an environment where land values have conservatively doubled in the past decade?

Corporate interest in Agriculture has always existed and gained momentum in the 1990's via Managed Investment Schemes (MIS) to provide taxation alternatives to investors e.g. Blue Gum Plantation and Olive Groves. Despite the demise of these schemes and the tax law amendments the corporate investment into Australian Agriculture continues. I was interested in examining some corporate farming models and determining how the family farming unit can attract external capital as a method of future farm business growth and expansion.

Why corporate farming is attractive in Australia

Corporate farming is a term that describes the business of Agriculture, specifically what is seen by some to describe the mega-corporations involved in food production on a very large scale. Corporate farming is often seen as the enemy of family farms.

It has a tendency to concentrate food production through the adoption of methods which are designed to maximise output. This is then exploited via a process of vertical integration.

The intensive forms of agriculture have been the initial participants of Corporate Agriculture and vertical integration.

The chicken meat industry is a prime example in Australia where two large, integrated, national companies supply more than 70% of Australia's broiler chickens.

Extensive Agriculture has now begun to be attractive to corporate funds.

In examining alternatives to debt financing the farming operation and expansion the question needs to be asked; why would the corporate companies want to invest in Australian Agricultural land? Some of the reasons are as follows:

- Secure land ownership
- Export orientated production
- Established infrastructure (storage, roads, ports etc)
- Safe high quality food products and commodities
- Increasing global demand
- Sustainable production methods
- Rapid technology adoption
- Skilled labour and management

- Best practice systems
- Modern, state-of-the art machinery

Currently Australia agriculture offers all these advantages, few countries can compare.

Financial returns

Given the current global financial issues, all the stakeholders in the supply chain, such as

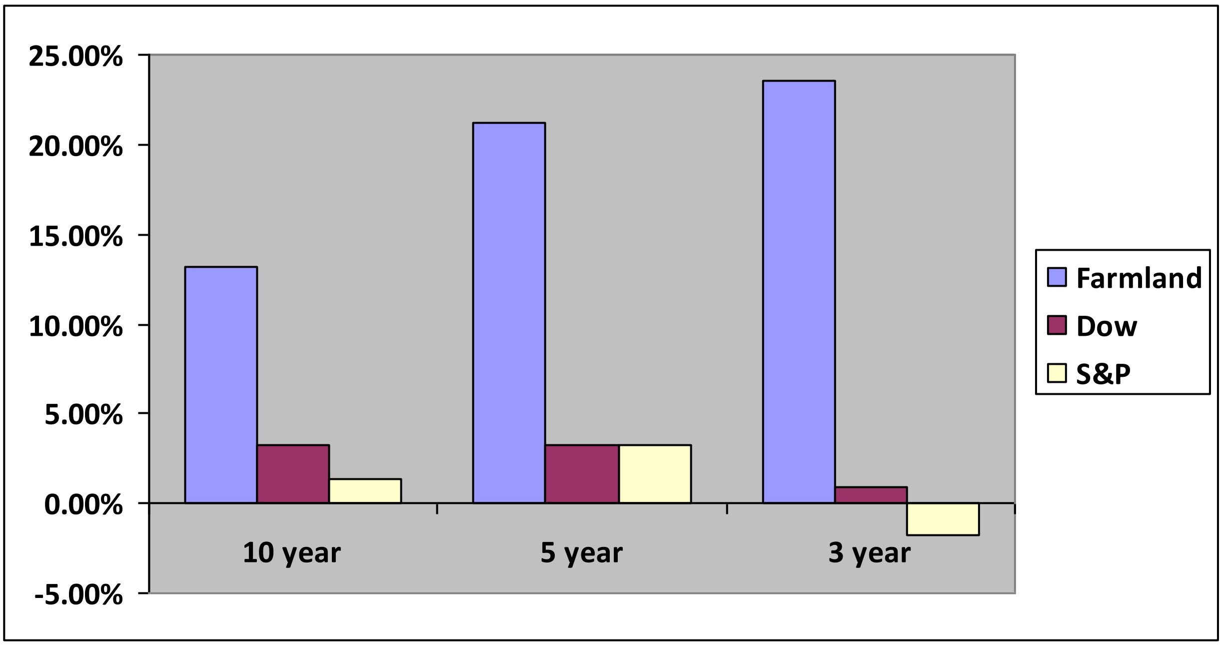
- players in the finance and food industries,
- the investment houses that manage workers,
- pension/superannuation funds, private equity funds looking for a fast turnover,
- hedge funds driven off the now collapsed derivatives markets,
- grain traders seeking new strategies for growth

are turning to land to provide both food and fuel production as a new source of profit. Land is not a typical investment for these investors.

Both the food and financial crises combined have turned agricultural land into a new strategic asset. Statistics from the US show that farmland has produced an average return of 11.6% a year since 1951 (income and capital gain) with half the volatility of the stock market (Stookey and Laperouse: 2009)) while the S&P 500 index has produced a gain of 11.8%.

Within the last three to four years there has been a surge in interest in agricultural land investment among institutional and family investors. This is based on a number of factors:

- Strong long-term fundamentals
- Attractive historical returns
- A mix of current income and capital appreciation
- Returns which are not correlated to the financial markets
- A strong inflation hedge



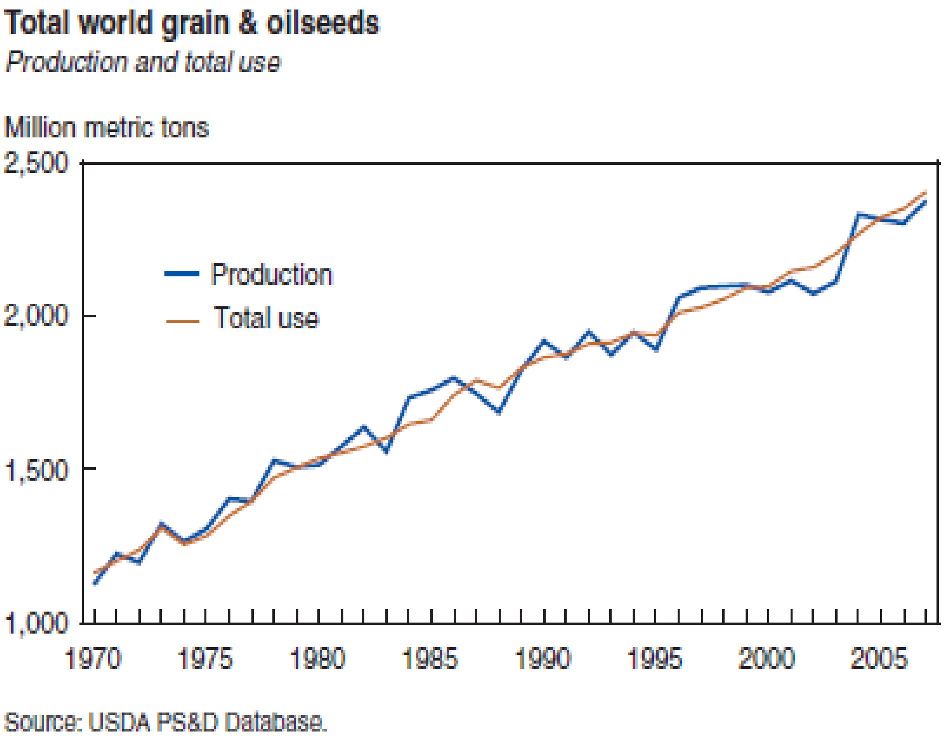
Source: NCRIEF index for period ending December 2008

In the US a majority of institutional landholders are members of the National Council for Real Estate Fiduciaries (NCREIF), which tracks total returns for farmland investments on a quarterly basis. For the 10-year period ending December 2008, the NCREIF index shows an average return of 13.2%. Land investments provide current income in the form of either lease payments or from the sale of crops.

Growing world population, rising incomes in the developing world and the increasing use of biomass for bio-fuels and for industrial applications is forecast to drive unprecedented growth in demand for agricultural crops over the next decade and beyond.

Food security

A number of countries which rely on food imports and are worried about tightening markets are seeking to outsource their domestic food production by gaining control of farms in other countries. They see this as an innovative long-term strategy to feed their people with far greater security. Demand for food is soaring. The world has consumed more than it has produced in nine of the last 10 years. World population figures passed six billion in 1999, are currently seven billion and forecast to reach nine billion by 2050, and possibly higher. The amount of arable land per person on the planet has halved in the last 40 years. S.G. Securities estimates that demand for grain alone will rise by 50% to 100% in the next 40 years and that we could expect to see a resource war by 2020 (USDA, 2010).



Hassad Food, the agricultural arm of a Qatari sovereign wealth fund, is investing throughout the world with the primary purpose of achieving food security for the Gulf States. Investments currently exceed $60 million of Australian agricultural land. Brazilian beef giant JBS now owns abattoirs and meat works in south-eastern Australia, and Singapore-based Olam International now controls almost 45% of Australian almonds (Cowie, 2011).

Australian Foreign Investment Policy

Australia is a capital-hungry country that has always relied on foreign investment as a driver of employment and prosperity in agriculture. Such investment plays an important role in maximising food production and supporting Australia's position as a major net exporter of agricultural produce, by financing investment, and delivering productivity gains and technological innovations.

Without foreign capital inflows, investment in Australia would be limited, resulting in lower food production with potentially higher food prices, as well as lower employment, lower incomes in the sector and lower government revenue. Foreign investment in agriculture supports agricultural production, job creation and contributes to the prosperity of rural communities and the broader Australian economy.

The sale of agricultural land in Australia is exempt from review under Foreign Investment Review Board (FIRB) regulations. There is rarely much attention given to the overseas purchases of farmland unless the purchased of assets exceeds the $231 million threshold. The FIRB examines each foreign investment proposal against a set of national interest criteria, including national security, competition, the other Australian Government policies, the impact of the economy and community and the character of the investor.

A Senate inquiry has been commenced into the effectiveness and operation of the 'national interest test'. This inquiry will examine a number of issues:

- The global food task and Australia's food security in the context of sovereignty.
- The role of the sovereign funds in acquiring Australian sovereign assets.
- How similar national interest tests are applied to the purchase of agricultural land and agri-businesses in countries comparable to Australia.

A range of environmental issues will also be pertinent to the inquiry, including access to future water resources; overseas demand for GM crops; the growing of crops for fuel substitution (e.g. ethanol) and the employment of local farmland as carbon sinks.

But is land ownership the primary reason for agricultural investment?

Global Ownership Laws – access to land

United State of America

To counter corporate ownership, nine states in the US have placed some sort of restrictions on Corporate-owned farms. Only two, Nebraska and South Dakota, have anti-corporate farming restrictions written into their constitutions. The other seven, which include Iowa, Kansas, Missouri, Minnesota, Oklahoma, North Dakota and Wisconsin, have statutes restricting corporate involvement in agriculture, though most include loopholes that dilute the impact of the ban.

The basis of these laws and restrictions is to encourage and protect the family farm as a basic economic unit.

Brazil

In August 2010, Brazil's Attorney General issued a new interpretation of the law restricting the purchase of farmland by foreigners to small lots. The hastily drawn-up document was a reaction to news that Chinese state companies and sovereign wealth funds were looking to buy large tracts of Brazils' interior (Stewart, Correspondent for the Progressive Farmer, 2012)

The process of constructing and formalising laws, which would restrict land deals but facilitate foreign investment in agriculture, is continuing. The complexity of the issue and wide reaching implications has softened the market for large lots of land due to the withdrawal of foreign-backed corporates.

Canada

Canadian land ownership laws have historically regulated that land is held by Canadian residents. The two main grain-producing provinces (Saskatchewan and Alberta) have laws related to ownership.

Saskatchewan

Saskatchewan is one of several Canadian provinces which restrict farm land ownership by non-Canadians. By limiting speculation in farm land and concentration of foreign ownership, the Act supports two major goals

- To maintain opportunities for Saskatchewan residents to acquire farm land in Saskatchewan for agricultural purposes.
- To support the development of strong rural communities in Saskatchewan.
- This Act affects non-Canadian individuals unless they are residents of Canada.

Alberta

Alberta also has laws protecting Canadian ownership:

- Foreign citizens and foreign controlled corporations may own or beneficially own up to two parcels of controlled and not exceeding 20acres in total.
- Defines a "foreign controlled corporation" as one in which the share ownership is 50% or more foreign or is effectively controlled by foreigners.

  (Note for public corporations with shares traded on a stock exchange in Canada, only shareholders owning 5% or more of the shares are taken into account, provided two thirds of the directors are Canadian citizens or permanent residents.)
- Trusts cannot be used to circumvent these controls

Eastern Europe

Western Commonwealth of Independent States (CIS)

Belarus, Ukraine, Russia, Moldova

The Western CIS countries, with the exception of Moldova, are still struggling over meaningful private ownership of agricultural land and the right to sell land, to mortgage land, and to use land to its best use without interference from the State.

All of the Western CIS countries are still primarily farming as large collective farms with little benefit afforded to individual landowners. Except for Moldova, few purchase and sale transactions are taking place, and the majority of those that do occur, even in Moldova, involve leasing back to the barely altered successors of the collective farms from which the land was allocated or divided.

For these countries, with the exception of Moldova, there is effectively no political will for reform, even though the farmers themselves are interested in a land market and land ownership. Recommendations suggested for the Western CIS countries are meaningful only to the extent the political situation in particular countries changes to allow it.

CIS Countries: Trans-Caucasus States

Georgia, Armenia, Azerbaijan

Azerbaijan, Armenia and Georgia are leading the CIS in terms of privatisation and farm reorganisation and are ahead of some of the EU accession states in these areas. The Trans-Caucasus plus Moldova are also much further along in terms of land market legislation and development of a land market. Each of these countries has the political will to privatise land and move toward a market economy.

They have developed some land management responsibility at a local level and have passed legislation clearly allowing for land transactions. Armenia and Azerbaijan prioritised privatisation and farm break-up and accomplished them simultaneously, with Georgia making significant inroads also.

Balkan Countries

Albania, Macedonia, Bosnia, Herzegovina, Croatia, Serbia and Montenegro, Kosovo

The rural land markets in these countries are not only influenced by economic transition issues, but also by ethnic strife, political instability and war. All of these countries have depleted both energy and resources that might have otherwise been directed in part toward land market development goals. In some ways, Albania leads in the kinds of reforms that could help to create a vibrant land and mortgage market.

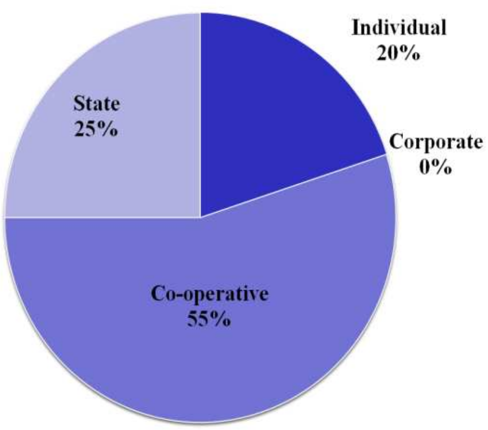
European Union (EU) Accession Countries

Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia

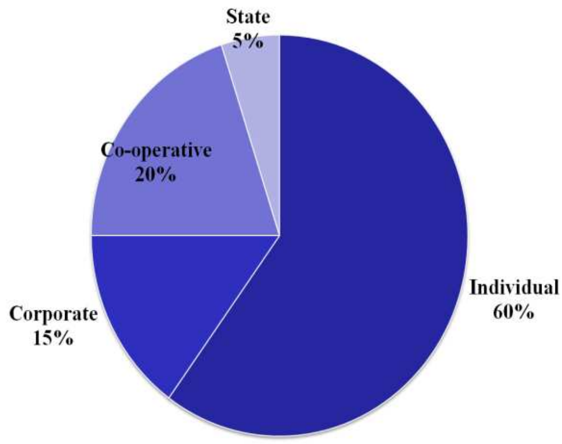
The EU accession countries have struggled less with the ideology of a market economy than many of the CIS countries, so privatisation of land was not disputed. However, in some cases, EU accession countries have chosen to continue support for large collective-style farms, and much less farm break-up has occurred in cases like Armenia, Azerbaijan and Georgia. It does appear that in countries where independent private farmers are not the dominant sector, the land market is functioning at a lower level than in countries with a larger number of private farms. Poland and Lithuania, for example, have an active land market while Hungary, the Czech Republic, Bulgaria, Slovakia and Latvia less active.

Central and Eastern Europe

Farm ownership pre 1990



Farm ownership post 1990



Source: Land Reform in Eastern Europe: Economic & Social Development Department.)

United Kingdom

The UK farmland market has a number of non-farming influences that contribute to its' complexity.

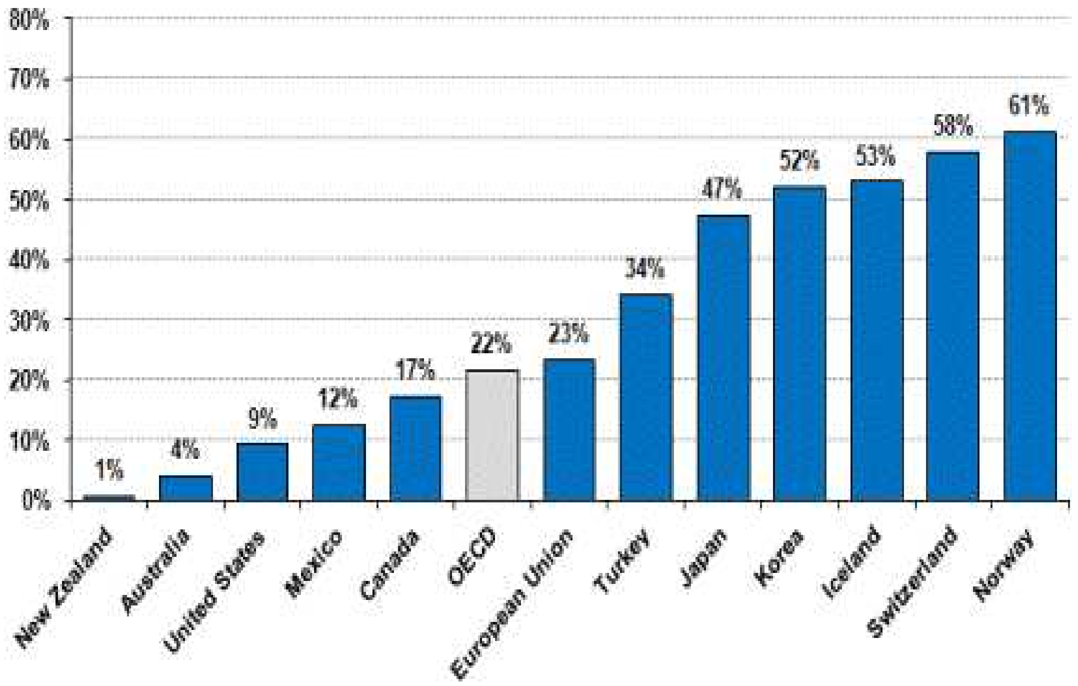
- The Common Agricultural Policy (CAP) which includes the Single Farm Payment.
- The taxation system – Farmland is exempt from inheritance tax, which can have a rate in excess of 40%. Agricultural land has become a tax shelter for the wealthy.
- Speculation in Rural/Urban development, changing farmland zoning into urban and industrial use.
- With a population of over 60 million, competition for land ownership is intense where the person to land area ratio is 270:1 ha whereas Australia has a ratio of 2.5:1 ha

Government support

Australia

Despite common misconceptions, Government support for Australian farms represents just 4% of farming income. By comparison, according to the Organisation for Economic Co-operation and Development (OECD), in Norway it is 61%, Korea 52%, in the European Union it is 23%, in Canada 17% and the US 9% (Dept of Foreign Affairs & Trade, 2011)

Producer Support Estimates as % of gross farm receipts, 2007-09



OCED, Agricultural Policies in OECD Countries: At a Glance 2010

European Union

European Union agriculture operates under a Common Agricultural Policy (CAP) which was introduced in 1957. The policy contains numerous parts and complexities which encompass all aspects of farming, environment, food safety, phyto-sanitory and animal welfare standards. A reform of this policy was introduced in 2003 and became known as the Single Farm Payment. This is a direct subsidy payment to landowners

This system of subsidy applies throughout the EU, according to rules agreed between the member states. However, exact details of implementation and grants vary from country to country, within the outlined rules. Transitional rules also apply for new member states which joined the EU in 2004 and more recently. States have a choice of whether to introduce the new scheme at once, or to phase it in over a period from 2005 to 2012. The UK Government decided to be one of the first countries in Europe to introduce the Single payment Scheme and phased it in from 2005.The Scheme is intended to change the way EU supported its farm sector by removing the link between subsidies and production of specific crops. (Financial Management in the EU, 2011)

United States of America

In the US, a subsidised, multi-peril, Federal Insurance program, administered by the Risk Management Agency, is available to most farmers. Payments to farmers for crop losses in 2011 exceeded $9 billion - the highest in American history (USDA, 2011).

Without crop insurance in place, the billions that have been paid out would have been required to be absorbed by lenders, input supplies, marketers and landowners.

Premiums paid by farmers and the Government have increased significantly as a result of insuring more valuable crops along with insurance costs. The Government pays about 65% of the total cost of the crop insurance program.

Direct payment subsidies are also provided to the farmers without regard to the economic need of the recipients or the financial condition of the farm economy. An example of this was the Energy Policy Act of 2005, where US corn ethanol subsidies were between $5.5 and $7.3 billion per year. Producers also benefitted from a Federal subsidy of 51c/gallon plus additional State subsidies that increased the total assistance to 85c/gallon. However this Federal ethanol subsidy was due to expire December 2011, along with the 54c/gallon tariff on Brazilian ethanol, (USDA: 2010).

Corporate Models

Investigation into Corporate Agricultural investment companies has shown there are four basic models. These include Company owned and managed; company owned and leased to farmers; management companies renting land, and production investment. There are other models being utilised that are more complex in structure which involves the existing farmer selling his holding into the parent company and operating on proportional investment/profit share. Due to the nature of this model the intricate details carry more confidentiality.

Company Own & Lease

These companies are predominantly funded by pension funds in the US who are looking to diversify their portfolio into agriculture to achieve long term stable moderate returns of approximately three to five% in annual returns and similar in capital growth.

Westchester Group Inc (TIAA-CREF)

<u>Teachers Insurance Annuity Association College Retirement Equity Fund (TIAA CREF)</u>

Westchester Group was established in 1986 in the United States. The company started with small farmland investor relations with TIAA CREF acquiring a controlling interest in Westchester Group in 2010. It is still a standalone subsidiary and remains independent and able to exercise its unique expertise and entrepreneurial approach.

Westchester is an agricultural asset management firm which provides a range of agricultural real estate and management services. It specialises in portfolio management and acquisition of farmland for institutional and corporate clients, individual farmers as well as individual investors. The company manages a diverse range of crops for its clients including crops such as almonds, wine grapes, apples and citrus, where the value of the asset is tied up in the permanent crop. Land that is utilised for row crop purposes (corn soybeans, cotton, cereal grains etc.) is rented to existing farmers where the asset value is tied to the land.

Westchester has an agricultural land portfolio exceeding two billion dollars, throughout the US, Australia, South America and Europe.

Westchester is a company that definitely offers opportunities to Australian farmers by renting land that they acquire, with a strong footprint in Australian agriculture having offices in Wagga Wagga and Narrabri in NSW, East Geelong in Vic and Perth, WA.

Hancock Agricultural Investment Group (HAIG) United States

The Hancock Agricultural Investment Group is one of the largest institutional managers of agricultural real estate in the US. It manages over $1.7 billion of agricultural real estate for institutional investors including public and corporate pension funds and corporate taxable investors. The HAIG land portfolio is predominantly in the US with smaller land investments in NSW and Qld in Australia.

The HAIG investment strategy is to acquire properties valued at more than one million dollars, investing in both row and permanent cropland. The company leases row crop properties or where it is advantageous to directly operate row crops, will do so to enhance returns. HAIG directly operates permanent crop land in order to maximise income returns but may choose to lease permanent cropland for clients looking for lower risk/return investments.

Assinboia Farmland Ltd Partnership (Canada)

Assinboia Capital Corporation is an agriculturally-oriented investment company based in Canada. Assinboia Farmland Limited Partnership was founded in 2005 and has acquired over 45,000 ha of Saskatchewan farmland, which is then rented by Canadian farmers**.**The objective is to attain long-term capital appreciation through increases in land value and generate a 2-3% tax-efficient annual yield for investors. The goal is to grow the portfolio fourfold over the next three to five years.

Currently in Australian agriculture, Westchester TIAA offers the most accessible farm expansion opportunity of all the models of corporate investment. Westchester TIAA employs a variety of structures in making its farmland investments with a focus on acquiring ownership in the underlying land. The company partners with farmers in the form of lease arrangements for the purpose of row cropping grain production to effectively manage the asset. The outcome for the investor is in the returns in the form of annual cash rental and capital gain in land value. The goal for farmers leasing additional farmland is to improve the businesses return on equity. The benefits of traditional leasing arrangements with corporate investors or retiring farmers have been reduced in recent years due to the large increase in land values. Landowners expect an annual cash rental reflecting a 3-5% return on the value of the land asset. Lessees are also exposed to climate variability, cropping input costs and a volatile global grain market; these are the real risks associated with leasing.

This model is used extensively throughout the Mid-West and Mississippi delta in the US, and likewise in Canada with Assinboia Capital. Whilst this gives farmers great opportunity in achieving farm expansion both the US and Canada have Federally-backed insurance schemes that dramatically reduce farmers’ exposure to large operating losses in poor seasons or low commodity prices.

Australian farmers operate without an insurance policy that covers production and price losses, which means their level of exposure to risk is inherently higher. Farmers do not want to have excessive amounts of their business under this model unless the production side can be offset by perhaps using the AACL model to limit possible large losses.

Westchester's model achieves its return to the investor through capital increases in land value so their investments tend to be acquired in the more reliable farming areas that have less exposure to variable seasons, which can have a large impact on land values.

Own/Lease & Manage

In this structure the Company invests in the land purchasing properties, either freehold or leasehold. They also access land by leasing properties on a short or long term basis. The companies that employ this model provide strong competition to local farmers when accessing land in the areas they target. The effect of this can underpin land values. To achieve their economies of scale, properties are aggregated which can lead to inflated land prices. Family farming businesses are often unable to compete due to the required rate of return disparity.

Positively, these companies also offer opportunities to farmers through contract arrangements. Some companies prefer to have minimal capital invested in machinery and pay commercial contract rates for operations undertaken, such as seeding and harvest. Warrakirri in WA uses this method.

Macquarie (Paraway Pastoral)

Paraway was borne out of the concept to form an Australian Pastoral Fund that was tailored specifically for global and local institutional investors. The aim was to provide a fund that captured all of the investment benefits of agriculture. The fund was founded in 2006 and in 2007 began acquiring properties in Eastern Australia. Paraway Pastoral is an operating entity of Macquarie Pastoral Fund.

Paraway has become one of the largest pastoral owners and operators in Australia with a total combined land holding of over 3.5 million hectares. Paraway has purchased 30 properties and has aggregated these into 17 pastoral businesses running approximately 220,000 cattle and 240,000 sheep. Paraway operates all properties with company staff. These properties lie in three diversified rainfall zones including Northern Australia and Northern and Southern NSW.

Wellard Agri

Wellard Agri is the production-focussed subsidiary of the global Wellard Group. Through the process of vertical integration they are able to control food safety and security.

Wellard Agri has a property portfolio of 34,000 ha of company owned land, and leases a further 15,000 ha throughout the agricultural areas of Western Australia. The company is amongst the top 10 grain producers in Australia and has large beef and sheep enterprises, including ram production and genetics for farmers across Australia.

Warakirri Asset Management P/L

Warakirri is an asset management business established in 1993. It is a private company, 100% owned by its directors and staff. Warakirri provides specialist investment vehicles to meet the needs of charitable, professional and institutional investors, Australian Equity funds, Australian Agricultural funds and currency management.

Warakirri's initial agricultural investments were into broadacre cropping totalling 65,000 ha in Victoria, Southern and Northern NSW, Southern Queensland and Western Australia. In 2006 the company established Warakirri Dairy Industry Trust running 7,500 cows and 3,000 heifers. It is now in the top 10% of grain producers in Australia and the top 5% for milk production. Warakirri is owned and managed with company staff.

Sustainable Agriculture Fund

The Sustainable Agriculture Fund (SAF) was launched in 2009. It is an unlisted investment fund which owns and operates farms throughout Australia. The fund targets institutional wholesale investors and directs funds into Australian farming both in terms of land ownership and husbandry. SAF is managed by Australian Funds Management P/L (AFFM) which is majority owned by its' executive staff. The base management fee is only paid to AFFM if the income is aligned with the top 25% of producer incomes. No returns are paid if profits are negative and performance is not paid on capital growth, additionally there are no fees paid on acquisitions.

Magyar Farming Company Ltd (Hungary)

Established in 1998, Magyar Farming Company is a business based in the UK. Current farming operations are established in Hungary, Serbia and Ukraine. The initial investment was in a former state farm in Hungary and later in a former state farm in Serbia. Along with these investments, land is rented to increase the land area farmed. Magyar employs predominantly a local workforce, situated principally in cereal production as well as producing irrigated potatoes (including storage and packing) and a large dairy herd supplying the Hungarian liquid milk market.

This operation is managed by Andrew Hunter (1996 UK Nuffield Scholar) who is based in Hungary.

Prime Agriculture Australia Fund

The Prime Agriculture Fund (Prime Ag) is a company that has been established to provide investors with an ASX listed vehicle that invests in select Australian rural properties, some with attached water entitlements.

Prime Ag aims to take advantage of expected soft commodity price appreciation as well as the anticipated capital growth from these properties and water entitlements. The company strategy is to achieve a diversified commodity exposure by establishing “hubs” across a number of different geographical regions in northern NSW and Qld. This implementation will help achieve economies of scale and crop diversity.

Black Earth Farming (Russia)

Black Earth Farming (BEF) was established in 2005 and was among the first foreign-financed companies that undertook considerable investments in the Russian agricultural sector. As of 31st December 2011, BEF has 318,000 ha under control of which 82% is fully owned with over 230,000 ha cropped.

The company raised initial funding from the family backed Swedish investment companies Vastok Nafta and Kinnevik. BEF completed an Initial Public Offering (IPO) in December 2007.

Shares were listed in the form of Swedish Depository receipts, on the OMX First North Exchange in Stockholm. In June 2009 the company changed listing to the NASDAQ OMX Stockholm where the shares are currently listed under BEF SDB.

During the first years the company’s main focused was on acquiring and obtaining full freehold ownership to agricultural land. Black Earth Farms is now in the final stage of the process of registering land into ownership and is now focused on raising productivity of the current asset base, having heavily invested in large, modern machinery and significant storage infrastructure.

Production Investment

AACL

Grain Co-Production (GCP) is effectively an extension to the Australian ethos of sharefarming and is highly accessible to farmers. Investors provide funds to grow wheat, barley or canola crops and growers provide the land, equipment, inputs and expertise. The risks and rewards of growing the crop are shared by the grower and investor with growers rewarded for outperformance.

AACL is an unlisted public company, incorporated in 1997 to attract investment into the WA grains industry. Through the development of the Grain Co-Production concept, AACL has provided a vehicle for investment in the wheat industry in addition to providing benefits to famers through a risk-sharing structure. Grain Co-Production (GCP) is effectively a cash-flow and income protection product and is the only product of its kind available to Australian grain growers. Grain Co-Production provides growers with a guaranteed amount of income on a contracted area of their farm each season. The majority of the payment to growers is made at seeding time, underwriting their cash-flow regardless of the season.

Should the contracted crops underperform or fail then the investors incur that loss, not the growers. As such, the investor's funds provide a form of income protection to the farmer by sharing the risk of the crop with the investor. If there is no production then the farmer is not liable to pay back the costs, although rates for capital are slightly higher than conventional lenders if there is a crop offsetting AACL's risk. Farmers use this product as a means of hedging against production risk, in the absence of a multi-peril insurance product. However, AACL is not a lender of last resort. The contracted farmers are assessed on their capacity to grow a crop and how well they can manage crop production before being accepted. AACL contracts crops in many different locations and pools the result in order to manage the investor's risk of growing grain in one location.

In better seasons the growers will give up a considerable amount of income to the investor; however the grower will experience more consistent year–on-year cash-flow over the long term. By stabilising cash-flow, regardless of the season, AACL enables the grower to make more proactive decisions knowing that their downside risk is effectively covered.

A key feature of the AACL model is that it provides incentive for key participants in the project to perform. The incentives are aimed at maximising returns to growers by providing rewards to participants for performance. A harvest bonus is payable to growers when there is a harvest surplus. This arises when the value of the harvested grain from a co-production unit (CPU) exceeds the first performance benchmark known as the target value. Farmers that have a net income result that is higher than the target value amount, as set out in their GCP contract, will qualify for a Farmer Performance Payment. These payments are distributed from grain marketing revenue earned by AACL as the GCP Project Manager. The 2011 project required a minimum investment of six co-production units or $26,400 including GST. The applicants can increase their initial investment in the project in increments of six co-production units.

In addition to providing farmers with income protection through up front, non-recourse funding, participating in GCP is also a commitment to participating in AACL's grain marketing.

Deregulation in the Australian grains industry and increased volatility in the international grain markets has meant that having facilities to actively hedge grain and provide access to markets, both domestically and internationally, is more important than ever.

GCP grain is managed by grain marketers at AACL, in partnership with the trading team at Glencore Grain Pty Ltd (Glencore). AACL and Glencore work together to achieve the marketing objective of ensuring the best possible return to farmers and investors.

The cost and structure of the product is continually evolving in order to meet both farmer and investor requirements.

Management Companies

The companies employing this model are solely focussed on obtaining returns from production profits, sometimes via a profit share arrangement, as with Velcourt UK. These companies are based in countries that have government support programs to mitigate risk to both price and production. The evolution of this model was in a large part due to legislation permitting corporate investment in freehold land as in Canada, or where landholders desire to retain land ownership as in the UK.

This model would be less attractive to companies or individuals in Australia with the absence of government support underpinning production security.

Velcourt (United Kingdom)

Velcourt started its farming operations in 1967 farming land which belonged to other landowners. It is a farm management company that is financially rewarded by a share in profit generated – a genuine partnership. In 1975 the company formed their own research and development department and have used this as leverage to access land throughout the UK.

Velcourt have been involved in project management in Africa (Zambia) with the Commonwealth Development Corporation, Eastern Europe and most recently Russia and the Ukraine. Velcourt is currently farming 55,000 ha in the UK of which there are 11 landowners on three – five year lease terms. The largest of these is 3,040 ha and the smallest 40 ha.

Pike Management Group (Canada)   Broadacre

Pike Management Group (PMG) is a producer focused management services firm. Based in Calgary, Canada, the company offers farmers commodity market analysis and discussion along with farm management advice.

In 2010 PMG created a division called Broadacre via institutional investment funding. The company invests in land rental and production in the State of Saskatchewan primarily in broadacre crops (canola, chickpeas, wheat, yellow peas, and lentils). The scale of Broadacre Agriculture now encompasses more than 30,000 ha of crop production.

One Earth Farms Corporation (Canada)

One Earth Farms (OEF) was established in 2009 and operates as a subsidiary of Sprott Resource Company. OEF is a unique company that has based their business plan on an alliance with the First Nations (Indigenous) in Canada. The First Nations people of Canada control large tracts of land that historically have been rented to Canadian farmers or run by indigenous landholders. One Earth Farms has entered into longer term lease arrangements, offering employment opportunities to the native Canadians, land care programs, and paying market price, all of which had been lacking in previous times. Since 2009 the OEF operation has expanded to exceed 80,000 ha of cultivated land and pastoral properties.

These Canadian companies are now looking at agricultural production as a positive investment vehicle for investors owing to global food production insecurity causing positive grain price volatility. The scale of these investments and the risk associated with crop production is somewhat mitigated by geographical spread of the operation and the existence of a federally supported crop production and price insurance scheme.

Conventional methods

Share farming

A share farming agreement is an arrangement whereby a landowner or person in possession of land grants a farmer control in order to cultivate the land. The profits and/or produce derived from the farmers' cultivation are shared between them in proportions agreed between the parties.

The income and cost sharing arrangements detail how the costs and income are to be shared between the landowners and tenant. Different crop share farming agreements have significantly different risk profiles e.g. a 50:50 agreement which shares costs and returns equally to a 30:70 agreement where the landowner incurs no direct costs and receives 30% of net returns.

Taxation implications and benefits for landowners in sharefarming are greater than leasing agreements; however, they carry a higher percentage of risk.

A combination of leasing and proportional sharefarming can have greater net benefits to both investor and farmer. For example a lower annual cash rental of between 1% and 2% with the investor participating in some production risk but also benefitting in potential upside on yield and price outcomes along with the tax benefits of direct cropping costs. The benefit to the farmer is seen a reduction in production risk and operating costs.

Contracting

In addition to sharefarming and leasing the option of contracting is available to farmers requiring additional land to justify the purchase of modern machinery to improve efficiency and profit from their existing land holding. An example would be variable rate technology, auto-steering capabilities, Weedseeker® and Green-seeker® technology.

Contracting is used extensively throughout the UK, Europe and the US. Several large corporate farming operation in Australia utilise this service for the operation of their farming business. Warrakirri is one Australian example and are currently advertising for applicants for the provision of these services for their farming operation in the Eastern wheatbelt of WA.

For large corporate owned farms this can be the most efficient and economic method of operating the business. One manager can oversee the critical seeding, spraying and harvesting operations and not be responsible for staffing, maintenance and the capital outlay in machinery purchase.

Conclusion

Australian farmer access to corporate capital is limited by size of property, geographical location, return on equity and individual farmer's capacity to integrate models. Central to corporate investment is size of operation to achieve economies of scale, implementation of new technology and market access.

Farm profitability and risk to the family farming business was the cornerstone to this study of corporate farm businesses and models throughout the world. If these key parts of farming were not being so strongly challenged then alternatives to financing and protecting a family business would not be as attractive.

However in all farming sectors, whether it is broad-scale grain farming, dairy, beef or horticultural, farm profit levels are minimal, while at the same time there is unprecedented demand for investment in agriculture for many of the reasons already outlined in this report.

The challenge is for both parties, both the investor and the farmer, to mutually benefit from any collaborative investment. The issues of Government support can have a major impact on investor sentiment and likewise farmer interest or uptake of corporate investment.

With most corporate-backed funds, the scale of the investment is generally aimed at the larger businesses, so in most cases farmers' opportunities for co-investment or business relationship is restricted to family farming operations that have the capacity or willingness to operate with scale. A much higher level of business reporting and accountability are required with farming operations working with external capital.

The number of current opportunities to family farming operations is still quite limited, with corporate investors being quite specific regarding location and how they will invest. During this study it was evident that a number of companies were looking at Australia as a destination to invest in agriculture not specifically for land ownership but ultimately for food production. This means capital is not required to be tied to land but to food production itself. It is these opportunities I see having the real benefit to Australian farmers in the future where production has become our biggest risk.

Any recommendations to family farming businesses currently revolve around two opportunities that have significant presence in Australia. These are Westchester and AACL.

1. The Westchester business and model works on a similar principle as leasing land from an existing farmer wanting to cease farming operations but retain ownership of the land asset. A fixed rental rate and term are agreed upon and there is a formal lessee/lessor arrangement. Westchester has offices in most states of Australia and has very significant investments. This opportunity will not be available to all farmers because Westchester is specific about which regions they invest in and the scale of the investment also plays an important role.
2. The AACL – Grain Co-production model is an innovative method of growing grain. This investment opportunity enables investors to participate directly in the Australian grains industry

through the process of grain production. By subscribing to co-production units, applicants become a wheat, barley and canola producer or grower.

The funds provided by investors in GCP increases the farmer’s cash-flow and replaces part of their normal seasonal borrowings to ensure that farm equity is protected. By reducing the level of peak debt and providing guaranteed cash-flow, GCP enables farmers to better utilise their borrowing capacity to drive a range of business objectives, such as farm expansion.

With all external capital being invested into farming operations, particularly in production, the level of reporting is critical to the investor. In most cases the individual investors have limited knowledge on production systems and decision making that the farmer employs to achieve the greatest financial outcome. Many decisions a farmer makes have both long (5 – 10 years) and short (6 – 12 month) term implications.

For the investor to be confident that their financial interests are being maximised, it is imperative they are informed and educated in the farming process.

Farmers must be comfortable that an investor has long term commitment to the business model so that plans can be enacted to gain the greatest immediate and longer term financial outcomes for both parties.

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Plain English Compendium Summary

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Objectives	Investigate examples of corporate farming businesses: • Their business models • What influences their purchasing ability • Why Australian farming is attractive to overseas investors • How family farming businesses can gain access to corporate investment in agriculture
Background	Traditionally Australian farming has revolved around family farming operations. Global influences have placed agriculture as an attractive and secure investment for global superannuation and pension funds as well as Sovereign wealth funds for governments concerned about food security
Research	Research was conducted by visiting companies in the UK, Eastern Europe (Slovakia, Hungary, Serbia and Romania) New Zealand, US, Mexico, Canada, Brazil and Australia
Outcomes	Corporate models exist currently and Australian agriculture is well placed to attract more capital. There will be multiple investment opportunities which will benefit both the investor and farmer.
Implications	A greater number of farmers will own a smaller percentage of the land that they operate.