THE PROFITABILITY OF FARMLAND AS AN ASSET CLASS

BLUE HARVEST. The liberalisation of the Danish agricultural market provides interesting investment opportunities to foreign investors.

Jens Ohnemus
CEO, Blue Harvest

Danish agriculture is the European leader in terms of Farm net value added (FNVA) per Annual Work Unit (AWU)*, according to the 'EU Farm Economics, 2012' report. Three years ago the government liberalized the sector and opened up the possibility for non-Danes to acquire a farm in Denmark as long as the farm remains cultivated in accordance with existing regulations.

The price of Danish farmland has fallen by 40 to 50% since the peak in 2008, and is now at 2006 levels, costing around EUR 16'000 per ha, compared to 24'900 in the UK or 18'900 in the corn-belt in the United States. The expected direct yield is between 3% and 7% depending on the case, for an IRR (Internal rate of return) of between 7% and 12%.

Jens Ohnemus, CEO of Blue Harvest, explains that this asset class is market-uncorrelated and offers an inflation hedge.

The latest legislative changes have opened the possibility for foreigners to acquire farms in Denmark. This was already the case in the UK where prices of farms have increased sharply. What advantage does Denmark offer to a private equity investor?

The Danish and the UK markets are similar in that they are so-called mature markets. However, there currently exists a window of opportunity in Denmark. The Danish banks were faced with a credit crisis in 2008, which resulted in many farmers being forced to sell their farms, even though these farms were profitable at the time. This caused a temporary but drastic drop in the price of agricultural holdings.

For Private Equity investors, farmland investments are interesting as the structures are transparent and the risks can be controlled. If the farm is fully operational at the time of purchase it can be profitable from the first year of investment, which is not the case for most other Private Equity investments. Another factor that should be taken into consideration over the long-term is the rarity of this kind of asset, especially in view of projected global demographic changes and the vital need to invest in the agricultural sector.

According to the latest FAO report, agricultural output needs to increase by 70% by 2050. Feeding the expected world population of 9.6B represents one of the biggest challenges facing humanity in the years ahead. In Denmark, more that 60% of the territory is dedicated to agriculture. Denmark is a net exporter of cereals, dairy products and pork; its agricultural output could today feed 20 million people, or four times its current population.

Denmark is one of the few countries to meet or exceed the requirements of the Kyoto Protocol: 25% of energy should be produced from renewable sources. Sustainable investing increasingly appeals to institutional investors. How does Danish farmland align with these criteria?

Indeed, renewable forms of energy (wind, sun, biomass) are one of Denmark's great strengths. Many farms now have their own 'green' energy production facilities. These are long-term and profitable installations, yet they do not encroach on the arable land area.

Blue Harvest respects the Principles for Responsible Investment (PRI) as recommended by the UN.

How do you assess the value of farms and farmland as an asset class?

A well-managed farm will always increase in value. The selection of the farm is the key factor. This involves examining the farm's history and the choices that have been made by those cultivating the lands to conserve the value of the land and to improve on the holding. An in-depth analysis is important, as improving the quality of the arable soils on a farm that has been mismanaged is a long and labour-intensive process. On the other hand, purchasing a farm that has been cultivated properly but poorly managed from an administrative point of view, can be a lucrative investment. Machinery and technology that is current and well maintained adds significant value to a farm; technology is one of the key drivers for good returns on a farm. Finally, costs can be reduced through sharing agreements with the local agricultural community for machinery, equipment, and maintenance. These arrangements can lead to important economies of scale.

Please explain the major steps involved in the investment process. What is the price of entry?

Our investors - private equity funds, institutional and individual investors - make a direct investment and become owners of their farm. Blue Harvest, as a member of the supervisory board of farmers, is the project manager and manages the acquisition process and negotiations with banks or credit institutions. Farms vary in price from two to 25 million francs, depending on the size of the holding (between 100 and 500 hectares), with an entrance ticket of two million francs.

How many farms do you currently offer for sale?

We currently have 12 farms and two forests in the pipeline, for a total value of 150 million francs. Our Blue Harvest team in Denmark is continuously monitoring the market and negotiating with local farmers, bankers and lawyers, according to the demands of our customers.

Interview: Elsa Floret

Translated by Carl Ankarcrona/sowrite.ch from the original article in French published in **L'Agefi**, Switzerland 25.06.2014.

***Farm net value added (FNVA)** is equal to gross farm income minus costs of depreciation. It is used to remunerate the fixed factors of production (work, land and capital), whether they are external or family factors. As a result, agricultural holdings can be compared regardless of the family/non-family nature of the factors of production employed.

The value is given per **annual work unit (AWU)** in order to take into account the differences in the scale of farms and to obtain a better measure of the productivity of the agricultural workforce.