Saskatchewan Agriculture

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MINISTER'S OFFICE

PALLISER
FARMLAND MANAGEMENT

Palliser Farmland Management Corp.
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Regina, Saskatchewan
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7th August, 2015

Honourable Brad Wall
Premier
Government of Saskatchewan
Room 226, Legislative Building
2405 Legislative Drive
Regina, Saskatchewan S4S 0B3

Honourable Lyle Stewart
Minister of Agriculture
Government of Saskatchewan
Room 334, Legislative Building
2405 Legislative Drive
Regina, Saskatchewan S4S 0B3

Honourable Bill Boyd
Minister of the Economy
Government of Saskatchewan
Room 340, Legislative Building
2405 Legislative Drive
Regina, Saskatchewan S4S 0B3

Dear Premier Wall, Minister Stewart and Minister Boyd,

Re: Saskatchewan Farmland Ownership Consultation

Canada is already among the world's largest exporters of several major agricultural commodities, including wheat and canola, and plays a leading role in global exports of a variety of specialty products, including lentils, peas and oats. According to the Conference Board of Canada, *'The Sky's the Limit'*.[1] It is an exciting time for Canadian agriculture and an exciting time for Saskatchewan agriculture too. In their 2012 report, the Conference Board of Canada identified wheat, canola, cattle and lentils as major export categories where Canada (with Saskatchewan at the heart of its production) has a comparative advantage over other countries. In order to capitalize on that position and maximize the potential of Canada's food and agriculture industry the report puts forward six key recommendations. The first of these, and the most important in our view, is to *'Expand the sources of capital'* available to agriculture. The Conference Board of Canada concluded that too little non-bank capital flows into the agricultural sector at present.

With that as the backdrop, the current debate on farmland ownership here in Saskatchewan takes on even more importance. On July 23rd, an article in the Western Producer cited research from the Johnson-Shoyama Graduate School of Public Policy (of the University of Regina and University of Saskatchewan), which had assessed the change in Saskatchewan's farmland ownership profile from 2002-14 following the relaxation of ownership regulations in 2002. They found that over 13 years investors have bought, and now own, 1.44% of Saskatchewan's farmland. Rather than suggesting a problem, this research shows that there is modest interest in Saskatchewan agriculture from the investment community that we should be looking to cultivate and support to further develop the sector.

Surely we (and that means all stakeholders: farmers, policy makers, private sector etc.) should be looking at the huge potential of the Saskatchewan agriculture sector and working collaboratively with investors, particularly Canadian institutions, to increase the flow of capital into the sector to the benefit of farmers and farming communities. We would like to see investment throughout the agricultural value chain: in farmland, in primary production businesses, in agricultural infrastructure (e.g. storage, irrigation and drainage both on-farm and at a macro level), in technology and machinery, in processing facilities and in logistics.

[1] The Sky's the Limit: The Viability of Canada's Food Economy. Michael Burt, Erin Butler, Michael Grant, Jean-Charles Le Vallée (December, 2012). http://www.conferenceboard.ca/e-library/abstract.aspx?did=5129

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Palliser Farmland Management Corp. is based in Regina and works with the Canada Pension Plan Investment Board (CPPIB) in managing the farmland portfolio they own (via Assiniboia Farmland Holdings LP). Many members of our team, including myself, were born and raised in Saskatchewan and we are acutely aware of just how important agriculture is to our economy and our rural communities. Palliser has been actively focused on Saskatchewan agriculture for ten years, initially through our investments in farmland (for retail investors that we then sold to CPPIB) and more recently through our continued management of this portfolio on behalf of CPPIB. Over the course of the last decade members of our team have talked to many farmers in Saskatchewan and across the prairies, and in this submission we've tried to convey the important messages that we continue to hear and put forward a number of pragmatic ideas that might pave a road towards a better and brighter future for agriculture in Saskatchewan.

1: Does outside investment in the farmland market help or harm farmers?

The two main arguments being levied against outside investors and, more specifically, pension plans and investment trusts have been: (i) that the price of land is being bid up as a result of the 'big pockets' of these groups, meaning that local farmers can no longer compete; and (ii) that farmers need to retain equity in their land to weather difficult years. Saskatchewan Farmland Security Board data shows that outside investors are not bidding up the price of land. Many farmers continue to value choice in how they finance their businesses, with the flexibility afforded by rented land a key part of their strategy.

Is the price of farmland being bid up by outside investors?

An assessment of Farmland Security Board data between 2010 and 2014 shows that ~98% of farmland transactions take place between non-institutional buyers, mainly farmers. Coupled with the fact that investors own only 1.44% of Saskatchewan's farmland, there doesn't seem to be any evidence to suggest that outside investors are driving up land prices. To the contrary, we have seen that farmers pay a higher multiple of assessment when acquiring land than non-farmers do. Our experience over the last decade at Palliser supports this view. We've always found it difficult to compete with local farmers because they attach a premium to farmland assets that are adjacent, or in close proximity, to their existing holdings. In recent years this challenge has become more extreme; after a number of years of strong commodity prices farmers have had the cash available to pay top dollar to purchase farmland. In the 2014 calendar year, we supported CPPIB in the diligence and acquisition of only three properties in Saskatchewan, despite looking at approximately 100.

Do farmers want to have all their equity tied into farmland?

Farming is a capital-intensive business and farmers have told us on multiple occasions that flexibility is crucial to success. Economies of scale deliver important efficiencies to farming operations, but achieving scale is a big challenge for farmers because of the capital investment required. Having long-term investors actively participating in the farmland market provides a healthy alternative for farmers looking to grow their businesses. Similarly we've seen a number of examples of young farmers getting started by renting land rather than owning.

A typical scenario that we've been approached on numerous times at Palliser is a farmer who has more equipment and manpower than needed on their current operation and as a result they decide to expand. The farmer identifies a farm that is strategically positioned, and contemplates two options: (i) buy the farm directly and take on some element of debt (it's unusual for farms to be bought with 100% equity / cash), which directly impacts their balance sheet and requires them to put their existing land holdings up as security; or (ii) partner with an investor, who will buy the land and rent it to the farmer through a long-term contract. In the second scenario, there is no impact on the farmer's balance sheet (barring the additional inputs required to grow a larger crop).

If it is a good season, the farmer's return on capital will be much higher than if they owned the land - beneficial to their equity. By contrast, if it is a bad season the farmer is only exposed to the additional input and rent costs, but not to the repayment or risk associated with the debt. Again, this would be better for their equity and their security.

The landlord-tenant model is not new. Rented land has played an important role in production agriculture across the Canadian Prairies for decades. In Saskatchewan, the proportion of leased land in farming operations has been between 35 - 40% since the mid-1980s, which demonstrates the importance that farmers attach to the flexibility it provides. This ratio has not changed even though investors have entered the market. In our conversations with farmers across the province, the importance of a 'balanced approach' to accessing land is prevalent. They look to incorporate both owned (through a mix of debt and equity) and rented land in their operations and as a result they place value on the role of outside investment in the farmland market because it limits the need for them to take on unnecessary risk by expanding their businesses using debt and thereby protects their equity.

Other positives from outside investment in farmland (and a diverse farmland ownership profile)

Not only does outside investment in farmland help to protect farmer's equity as exemplified above, it has other direct and indirect benefits that have not been discussed in the current debate:

Market stability: Having a diverse range of capital providers actively participating in the farmland market brings stability in turbulent times. Consider a scenario in which commodity prices soften and interest rates rise dramatically. Farmers are unlikely to have either the desire or the capacity to purchase farmland in such circumstances. If farmers were the only group allowed to buy farmland, the most probable outcome would be a significant fall in land values, which would erode the equity that farmers have on their balance sheets and cause problems with mortgage lenders. By contrast, capital providers with a longer-term outlook will continue to invest through these turbulent periods, which would support farmland values and help avoid another farm financial crisis - a desirable outcome for farmers and for policy makers. When Palliser entered the farmland investment space a decade ago, it was normal for a farm to take 2-3 years to sell. Many selling farmers have told us that without our presence in the market, it would have taken much longer to sell their farms.

A stepping stone to further investment: From our work with CPPIB over the past 18 months, we've developed a better appreciation of how institutions think about investment opportunities and how an initial investment can trigger other investment ideas. As part of our mandate, we have helped CPPIB to improve the farms they own in Saskatchewan by modernizing on-farm infrastructure, cleaning up disused yard sites and participating and investing in water management plans and Conservation and Development drainage projects. In addition, we have begun to explore broader investment ideas around irrigation, drainage and storage. These are conversations that have developed organically as CPPIB has gained a better understanding of agriculture in Saskatchewan having made their original investment at the start of 2014.

2: What option represents the best way forward for Saskatchewan's farmers?

Unfortunately, up until this point the farmland ownership debate has been far too narrow in our opinion. It has failed to look at the bigger picture and grasp the importance of much needed investment in Saskatchewan's agricultural sector. We have tried to take a much more positive viewpoint in looking for a pragmatic solution that can pave the way toward a better and brighter future for our farming communities, and in our deliberations we've assessed the pros and cons of three main options that we've summarized below.

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Option 1 - Remove the existing moratorium and open up the farmland market to domestic capital

From our conversations with farmers it appears that the main concern surrounding outside investment in farmland relates to non-Canadian ownership rather than the role of domestic institutions. In that sense, the existing legislation covers the main concern of rural communities. We strongly believe the direct and indirect benefits that accrue to farmers from having a diverse ownership profile for Saskatchewan farmland are considerable:

a) Adds liquidity to a market that is inherently illiquid
b) Offers support and stability to the market in turbulent times
c) Gives farmers flexibility in how they think about land and their operations (protecting their equity); and
d) Forms a stepping stone to other investment in the agricultural sector

Given that outside investors have purchased less than 1.5% of the province's farmland since the legislation on farmland ownership was last modified in 2002, nearly one and half decades ago, rather than looking to introduce additional restrictions, perhaps the best course of action is to look to open up the market still further. We believe in free markets, a belief that we share with the government, and although we realize that this option may not be palatable in the short-term, we hope that over the medium to long-term it will remain as a viable path.

Option 2 - Regulate the flow of capital into the farmland market

As we've watched the debate on farmland ownership unfold over the last twelve months we've grown increasingly concerned that the contemplated legislative changes to introduce restrictions on pension funds and investment trusts will only have negative implications for farmers and the province more generally. We feel that restrictions will undermine the current interest in Saskatchewan agriculture and jeopardize the long-term goal of unlocking the potential of the sector for the benefit of all stakeholders, but primarily the farmers. In addition, we have concerns that this approach will erode the province's excellent reputation as being open for business and open to investment to some degree, with implications for investment in the broader economy.

An alternative option, which we feel deserves serious consideration, would be to introduce a simple set of controls to manage and then monitor the flow of domestic institutional capital into the farmland market (e.g. an agreed dollar amount of investment each year etc.). This would be a way of appeasing the minority of stakeholders who are calling for restrictions, it would mitigate any damage to Saskatchewan's reputation and, crucially, it would keep investors focused on a sector that is desperately in need of investment. It would support the government's own Saskatchewan Growth Plan, which has ambitious objectives for increased agricultural production and exports from the province. It would enable the achievement of the objectives of that plan, which would be more difficult if investment in this key industry was restricted. To us, this seems like a reasonable position that delivers a win-win.

Option 3 - Impose a blanket restriction on institutions (in the form of Pension Funds and Investment Trusts)

As we've noted above, we feel that the option of making farmland ownership legislation more prohibitive through the introduction of a blanket restriction on pension funds and investment trusts (however they would be defined) would represent a huge step backwards for the farmers of Saskatchewan and for the province as a whole. While this option might generate some political capital in the short-term, we cannot identify any tangible benefits to farming communities. From our conversations with farmers, the call is for government, investors and the private sector to work together collaboratively to develop strategies and identify projects that will help drive positive change in agriculture. We agree with the Conference Board of Canada: the potential is undoubtedly there; we need to focus on unlocking it.

3: Conclusions

Before drawing our conclusions, we felt it important to comment on the consultation process and the timing of the debate. It is regrettable that the consultation process has been reduced to a basic survey, which we suspect only a fraction of stakeholders will complete. Unfortunately, human nature dictates that it will be the people who are angry or upset about the issue who put forward their opinion and it will be those who are indifferent to, or supportive of, outside investment that won't participate. Our hope is that the Ministry of Agriculture looks to complete a more comprehensive consultation after this process to evaluate all of the options before making its recommendations to the Cabinet.

Finally, we believe that the introduction of a framework to manage the flow of capital into the farmland market offers a pragmatic solution that would be readily supported by a majority of stakeholders. It gives the government the opportunity to work closely with investors in a controlled fashion to understand and monitor their investment strategy and explore other investment ideas. We would be more than happy to work with the provincial government and other stakeholder groups to talk about the farmland market and opportunities to help the broader agricultural sector develop.

Palliser Farmland Management Corp.

Per: ____________________

for: Laurie Powers
Senior Portfolio Manager