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MACHINERY AND LAND: TIME TO BUY?

Revised and Adopted for Ohio

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MACHINERY AND LAND: TIME TO BUY?

Cautious optimism pervades Ohio's community of grain farmers. Reduced debt, strengthened crop prices, and a host of forecasts projecting continued near-record income for '88 and '89 have buoyed the spirits of producers and agribusiness firms throughout the state. This good news has grain farmers again focusing attention on their favorite investments--land and machinery. Most grain producers are asking, "Should I repair or replace that piece of equipment? Should I rent or buy that 80 acres?"

MACHINERY

The pool of equipment on Ohio farms continues to age and sorely needs repair and/or replacement. The last year U.S. farmers, as a group, made a net addition to their equipment inventory (purchases minus consumption) was 1981. During the period 1976-1981, they spent an average of $12 billion per year on new equipment, an average net addition of approximately $1.5 billion per year. Beginning in 1982 and each year since, net additions have been negative, averaging $6 billion per year.

The '88 drought revised producers' thinking about equipment replacement. After a long dry spell, machinery dealers were smiling again--at least until June '88, when farmers stopped replacing equipment, tractors, and combines. Better-than-expected crops this fall and higher prices have re-stimulated purchases this winter, but not to the level dealers would prefer. Producers prudently continue to delay the replacement of "large ticket" items.

Farmers with debt outstanding will find that most of their questionable equipment can be repaired at reasonable cost and that any excess cash will probably be better utilized to reduce debt rather than trading up for new equipment. There will, however, be equipment that will require replacement rather than repair. Producers need to exercise their best judgment and put their mechanical skills to work when making the repair/replace decision. Taking on more debt when the future is clouded can create more problems than it solves. Good used equipment is becoming more difficult to find as the on-farm inventory gets older and fewer farm businesses liquidate. If, however, the opportunity presents itself, replacing aged and worn equipment with excellent/good used items will likely prove to be a good move.

The eternal question remains, however, "When is it more economical to replace than repair?" Many factors influence the repair/replace decision, and the answer is not the same for each farmer. The following "least cost replacement year" guidelines should be useful to each decision-maker.

EQUIPMENT TRADING GUIDELINES

Item	Minimum Cost Trade Year
Tractor	10
Planter	5
Combine	7
Other	10

It is important to keep in mind that these guidelines assume average usage and normal maintenance. Increased usage and/or poor maintenance will shorten the trade time. Most equipment will have a "least cost trade window" of three years when other factors such as cash and credit availability, etc. can be used to make the repair/replace decision.

LAND

The immediate past (1988) and the short and longer run outlook complicate land rental and purchase decisions. The lingering memory of crop losses in 1988 will temper the recent upturn in land rents and prices. The near term price outlook will, on the other hand, encourage some producers to bid higher rents and prices, as will the lower acreage reduction requirement for 1989. Higher input costs (seed, chemicals, and fertilizer) and lower target prices will tend to lower prices and rents. The longer run picture for expanding world production, lower loans, lower target prices, and lower market prices will likely stabilize farmland prices, if not cause a further reduction. The question is .. What to do?

Let's start with the purchase. Don't buy if it isn't necessary. Most of the returns from land go to operators rather than owners. Conversely, buy only if you have to and then only if you can do so mostly with cash. If you do buy, plan to have a minimum of one-third down. Fifty percent (1/2) would be better and would leave you in a more secure position to weather any economic storms in the near future. This year's drought will encourage operators to try to change from cash rent to share-crop rental agreements. Landlords, on the other hand, will want the opposite. If cash rental is the only option, producers must be clear in their minds what they can afford to pay. That means..don't get caught in a "bidding contest" with the neighbor, don't forget fixed costs, and don't work for zero wages. A reasonable cash rent for 120-bushel corn ground, allowing for a reasonable return for labor, equipment, and management, is likely to be in the $75-per-acre range for 1989. Paying more than this means some of the above inputs are not earning what is due.