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Trends in Land Values in South Africa

by

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Land and Agricultural Bank of South Africa

INTRODUCTION

The establishment of a sound economic farming policy in a rapidly developing country such as South Africa is closely related to trends in land values coupled with debt ratios.

Analysis of trends in land values requires, in the first place, an accurate understanding of the various purposes for which the values are determined, i.e. whether the evaluation is being made with a view to farming only, or for other purposes as well. Where the profitability of any particular property as a farming unit plays a secondary role, as in the case of valuations for taxation or expropriations, or where factors such as mineral rights, industrial development, etc. are additional considerations, the approach to the evaluation naturally differs from that applied where only farming is involved.

The normal concept of the value of land for farming purposes may be summarised briefly as that which a buyer would be prepared to pay and be justified in paying for a farming unit which, under normal farming conditions, would provide a reasonable living including all other benefits.

The most important consideration in the determination of the farming value accordingly depends on the estimated probable profits from the property in relation to foreseeable economic conditions and proper utilisation of the production capacity of the particular unit.

As it is the intention to deal in this article more fully with the trends in land values based on the true economic farming

value, the various circumstances under which other considerations should also be taken into account in evaluation, are enumerated briefly.

In the first place, land values are in many instances assessed on a basis which must comply with the functions of particular bodies.

In this regard one thinks of valuations for the Land Bank, for purposes of estate duty and income tax, expropriation or acquisition of land by the State, particularly where a new irrigation scheme or other development renders this necessary or valuations for Divisional Councils.

Even in these cases there is no standardised basis of evaluation: the basis differs according to the purpose for which the value is determined, as for instance contemplated compensation in the case of expropriation which also includes the factors of inconvenience, period of repayment of capital and rate of interest payable.

Where the period of repayment is long and rates of interest are low, the annual commitment is much smaller than the higher burden which results from a short term loan with a higher rate of interest. This is a factor which involuntarily affects the approach to evaluation.

On account of this, divergent evaluations for loan purposes of homogeneous units will consequently occur from time to time; because annual commitments which will differ in every case, will have to be taken into account.

In amplification of the foregoing, it can for example be mentioned by way of explanation that the Land Bank Act provides that the value of properties shall be determined according to their fair value for agricultural and stock-farming purposes, which is interpreted as the true economic value based on the actual production capacity of the property as a farming enterprise. In addition, this evaluation is related to the period of repayment, which normally extends over a long period viz. up to 35 years, and is not based on transitory or temporary factors which are caused by inflated values resulting from speculation, personal interests or a fluctuating demand for particular products.

Irrespective of how widely or narrowly this provision in the Act is interpreted, it must be kept in mind that the underlying intention of the legislation was to ensure that the long-term financing of the farming industry should be conducted on such a basis that the commitments under the debt can be met over a fixed period of capital redemption from the reasonable average income derived from agricultural products with a reasonable amount of working capital and the ability and knowledge of the applicant.

In the second place, land values for private investors who are interested only in the security and liquidity of their investments, are generally calculated according to prevailing trends which in many cases are of a speculative nature.

In the purchasing of land, there are also so many divergent factors determining the price, that in transactions of this nature economic aspects seen from a farming point of view, are seldom fully taken into account. Under such circumstances the policy in regard to the basis of evaluation will differ considerably from the concept of normal economic farming value.

In the third place, values are in certain cases influenced not only by the profitability of the farming enterprise: certain other considerations such as for instance exploitation of minerals, possible future

irrigation and industrial development come to the fore and determine the basis on which values are calculated. Here, personal opinions and speculation play a more important role than ascertainable facts.

Apart from the variable farming conditions and continuous new developments brought about by mechanisation and irrigation, divergent trends in land values are noticeable in all parts of the Republic, because of the different approaches as set out above. It is not possible to analyse and describe this aspect fully in a short article; and trends in land values since 1912 are therefore only given in broad outline from available statistics.

COMPARISON OF GENERAL TRENDS IN LAND VALUES IN THE REPUBLIC, 1912 - 1965

Graph 1 contains the following:

- (a) Average purchase prices per morgen of land in instances in which the Land Bank was involved, 1912 - 1965;
- (b) average transfer prices per morgen of all rural properties according to reports of the Bureau of Statistics from 1927/28 to 1963/64, and
- (c) average Land Bank valuations per morgen from 1912 to 1965.

The particulars under (B), which are compiled by the Bureau of Statistics, are obtained from the offices of the Registrars of Deeds and include properties not purchased for agricultural purposes, but also for various other uses, inter alia farms purchased for urban expansion and the exploitation of minerals.

The Land Bank is only concerned with land purchases for agriculture. Accordingly, if the average purchase prices and average valuations in graph 1 are compared, it is evident that since 1941 purchasers have throughout paid considerably more for land than the values as

determined by the Land Bank. During 1960 the average valuation was R22 per morgen, but purchasers financed by the Land Bank paid an average of R30 per morgen. During 1965 the average valuation was R30.50 per morgen and the average purchase price R43.90 per morgen, thus 43.93 per cent more was paid.

The extent to which the Land Bank grants loans is naturally determined by the security which buyers can offer, and the difference between the purchase prices and the valuations of property is accordingly not accepted or approved by the Land Bank. This is a matter for each purchaser.

Legend:

Average purchase prices in cases where Land Bank was involved.

Average transfer prices according to reports of the Bureau of Statistics, 1927/28 to 1963/64.

Average Land Bank valuations.

Attention must be drawn to the fact that graph 1 reflects an average and general trend in land values in respect of the whole Republic and not actual purchase prices in relation to valuations of the same properties.

The upward trend in land values from 1912 to 1945 as reflected in graph 1 was gradual and consistent in the case of both purchase prices and values set by the Land Bank in terms of legislation which had already been adopted in 1912 and which requires that only the economic farming value be taken into account.

Apart from less important economic factors, farming during that period was modelled on a more extensive basis and the average values fixed by the Land Bank followed, in broad outline, the open market trends.

The results of a realistic approach to land values can be clearly seen in graph 1, which indicates the effect of the depression during the years 1933/35, when Land Bank values were based on economic farming values and did not follow the downward trend shown by purchase prices nor the economically unjustified trend of increased purchase prices since 1948; but they did keep pace with the current inflationary trends, declining purchasing power of money and normal development in the sphere of farming. The downward trend in land values during the early sixties can be ascribed to the effects of credit restrictions, a succession of crop failures, natural disasters, increases in production costs, and declining price trends in some products during the preceding years.

As a matter of interest it may be mentioned that before 1933 valuations by the Federal Farm Credit Board for loan purposes in America were based on ruling selling prices, which led to fluctuating values being fixed according to changing economic conditions. During 1933 this policy was changed and it was decided that values should be fixed according to the normal agricultural value. This principle was incorporated in the 1945 Federal Farm Loan Act, which in substance corresponds with the basis of valuation already laid down in the Land Bank Act of 1912.

It is therefore clear that practical experience even in a country with a longer history of development such as the United States of America, confirms the principle that to ensure sound financing for farming purposes, land values for loan purposes, cannot be related to changing market values.

It may be mentioned here that investigation has revealed that the prices of the same properties which were bought and sold again in two homogeneous areas during the period 1959 - 1965, increased on the average by 64.7 and 60.7 per cent, respectively. However, in these areas the maximum price increases exceeded 400 per cent and these excessively high price levels are not reflected in the average transfer prices as shown in graph 1. The data must accordingly be regarded as reflecting trends in purchase prices and not as specific comparable cases.

As regards average purchase prices, it must be borne in mind that the Land Bank is involved in only a small percentage of all land transactions, and that it is accordingly possible that the data do not reflect the actual trends in respect of the whole of the Republic.

TRENDS IN LAND VALUES IN SPECIFIC AREAS, WHERE HOMOGENEOUS FARMING IS UNDERTAKEN

Graphs 2 and 3 have been compiled from statistics kept by the Land Bank and reflect the following:

(a) Average purchase prices per morgen in cases where the Land Bank dealt with applications, 1912 to 1965;

(b) average transfer prices per morgen of all rural properties as compiled by the Bureau of Statistics, 1927/28 to 1963/64.

Legend:

Average purchase prices in cases in which the Land Bank was involved, 1912 to 1965.

Average transfer prices according to reports of the Bureau of Statistics, 1927/28 to 1963/64.

Legend:

Average purchase price in cases in which the Land Bank was involved, 1912 to 1965.

Average transfer prices according to reports of the Bureau of Statistics, 1927/28 to 1963/64.

The average purchase prices of properties in graphs 2 and 3 show broadly the same trends in cases in which applications to finance the purchase price were received by the Land Bank and in actual transfer values in respect of all transactions during the period indicated. The greater difference, particularly in the Bethal district, from 1953 to 1963 can possibly be ascribed to the fact that with the development of the mining industry a considerable number of transactions took place at higher average purchase prices than those in which the Land Bank was involved.

A closer analysis of graph 2, compiled from statistics in respect of the Vryburg district, which was initially an extensive cattle ranching area, revealed that the uninterrupted increase in land prices discernible since 1946, can be ascribed mainly to the introduction of summer crops - which had previously been of little significance in the area.

In this connection research as indicated that of the 2,344 transfers of farm properties which took place from 1954/55 to 1962/63, only 563 properties (or 24.01%) were more than 500 morgen in extent. Approximately 76 per cent of the farm transfers were accordingly in respect of properties on which livestock was replaced as the major source of income by other agricultural products - mainly maize, kaffircorn and groundnuts.

The gradual sub-division of land and the rise in land values in the Vryburg district can also be seen from an analysis of statistics of transfer values as published by the Bureau of Statistics. During 1938/39 for example, 124 properties averaging 2,528 morgen in extent and R11.78 per morgen in value, were transferred as compared with 248 properties during 1963/64 of an average extent of 665 morgen and an average value of R24.88 per morgen. For the whole of the Republic there were 9,350 transfers during 1938/39, averaging 861 morgen in extent, at an average value of R3.94 per morgen - as compared with 10,630 transfers during 1963/64 with an

average size of 439 morgen and an average value of R32.16 per morgen.

As can be seen from graph 3, which is a summary of statistics in respect of the Bethal district, representative of a part of the Highveld devoted to the intensive cultivation of field crops, the extraordinary appreciation in land values started during the 1950's. This rise can be attributed partly to the increase in mechanisation and the cultivation of land previously used for grazing purposes only.

The prosperous years experienced, together with more favourable production results brought about by new fertilising programmes and the more efficient methods of cultivation resulting from mechanisation, were all factors which led to a greater demand and consequently higher purchase prices.

Analysis of graphs 2 and 3, representative of specific homogeneous areas, shows clearly that purchase prices increased moderately from 1912 until 1940, except for a definite downward trend, particularly during the years 1930 to 1933, which can be attributed to the results of the depression during that period.

The upward trend in purchase prices gathered momentum rapidly from 1943 onwards and soared at a disconcerting rate particularly from 1951, with a slight decline in 1960; thereafter the upward trend was maintained.

It is clear that in spite of fluctuating economic and climatic conditions, the considerable upward trend in land prices since 1951, cannot be ascribed to the prevailing inflationary trends and the profitability of farming alone, but that ready availability of credit coupled with the fact that agricultural land is becoming increasingly scarce, may also have been contributive factors.

GENERAL

Unrealistic rises in land values could, to a large extent, be counteracted if all

concerned with the financing of the purchase of farm properties were to follow a policy which took into account the economic value of the land, i.e. that in determining land values the likely profits to be derived from the unit should be the main consideration.

The question arises to what extent the sharper rise in land prices particularly since 1951 is the result, not only of a flourishing economy and depreciation of the value of money, but also of the trend to allow more and more land purchases to be made by means of credit financing. It is a pity that statistics in this regard are not available to enable us to determine the extent to which land price trends are also influenced by the availability of credit facilities.

The keeping of statistics to reflect trends in respect of purchase prices and

values presents certain problems, particularly if comparable data are required in respect of the same property, and particularly in cases where sub-division has taken place. Statistics in respect of transfer prices for homogeneous areas are not available either.

In conclusion, it can only be repeated that divergent norms of evaluation of farm properties by creditors cannot be conducive to a sound financial policy, and that in order to overcome this difficulty more attention will have to be paid to land value trends and the attendant debt ratio.

However, statistics in this regard are inadequate; and it is hoped that researchers and other interested parties will assist in filling this need in the future.

WHAT TO DO? - ONE MAN'S VIEW

The market is the connecting link between the farmers and the consumers of their products. Farmers expect the market to accept their products when they are ready to sell. Consumers take for granted that the market has anticipated their needs so that the products they want will be available in the quantities and qualities they desire at the time and place they are needed.

Prices become the crystallization of market operations. They help decide farmers' incomes on the one hand and consumers' costs on the other. Prices guide farmers in making their production plans. They help consumers in deciding on their purchases. How well the market meets its responsibilities is important to all of us.

Satisfaction or dissatisfaction with prices is a key to how well we think the market is doing its job. Let us keep in mind that our judgment on this score is not always accurate. We often blame the market for the unfavourable results which really are not its fault because they grow out of the conditions under which the market must operate. The responsibility of the market is to reflect conditions as they exist. To blame the market because the conditions do not please us is like blaming the thermometer or the barometer for disagreeable weather.

- O.B. Jesness. The Yearbook of Agriculture, 1954. U.S.D.A.