Farmland Investing Models

Is it better to lease to farmers or directly operate farms in uncertain economic times?

Canadian investors today are navigating a complex macroeconomic backdrop marked by persistent inflation, slower growth, and rising unemployment (often signs of a "stagflationary" environment). These factors have contributed to increasing investment interest in farmland, which stands out as a compelling inflation-hedging, defensive asset. Its appeal lies in its scarcity, potential for productivity growth and therefore long-term capital appreciation, and its potential to generate consistent, uncorrelated, risk-adjusted returns.

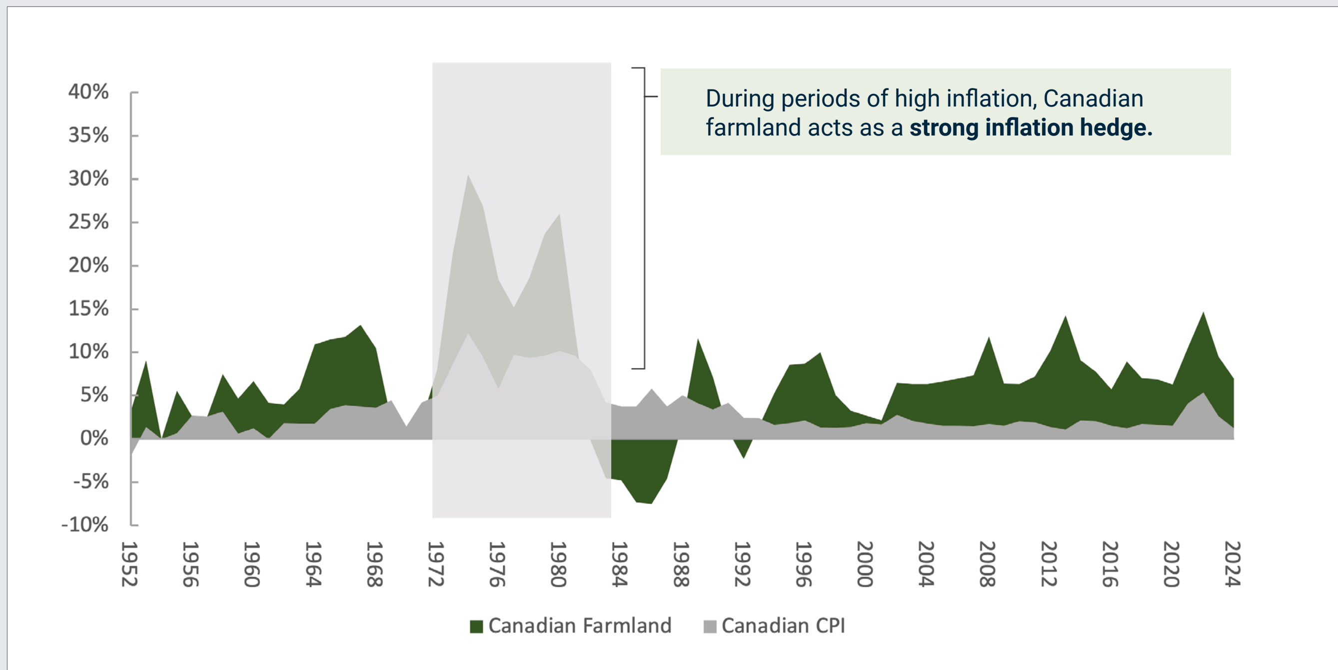
In this quarter's newsletter, we take a closer look at how economic conditions are evolving, why they matter for farmland investors, and how different investment/ownership structures perform under pressure. Specifically, we compare direct invest-and-operate models with invest-and-lease strategies to help investors better understand how each approach behaves in a stagflationary environment, assessing which approach can deliver stronger downside protection and better risk-adjusted performance.

Understanding the Current Macro Environment

Stagflation—when inflation persists despite slowing growth and rising unemployment—has re-entered the conversation across global markets, and Canada is no exception. In Canada[1] , GDP contracted by 0.4% in Q2 2025, even while core inflation remains elevated at 2.9%, and unemployment has climbed to 6.9%. At the same time, recent federal fiscal policy has leaned heavily on spending, with benefits unlikely to materialize immediately, potentially prolonging economic pressure.

In this type of economic backdrop, real assets with steady income and inflation protection, gain renewed relevance. Farmland has historically performed well in such conditions—but whether investors choose to own-and-lease farmland, or own-and-operate, can lead to meaningfully different outcomes.

Figure 1: Historical Performance of Canadian Farmland Values vs CPI[2]



Why Ownership Strategies Matter

When considering what method of farmland investment to pursue, two primary models dominate the landscape:

- **Direct Own-and-Operate Model:** Investors own and actively farm the land themselves (or take an ownership interest in the farm operator) to earn income from farm profits.
- **Sale-Leaseback Model:** Investors own land and lease it to third-party operators to earn rental income.

While both approaches offer exposure to farmland's long-term fundamentals, their risk / return profiles differ sharply, especially in challenging macroeconomic times.

In theory, the direct operating model should result in higher investment returns as a result of the investor taking on more risk by sharing in the operating business' profits. In practice, however, this model exposes investors to greater volatility due to operational risks, commodity price fluctuations, and weather-related factors. Considering the risks discussed above, along with the asset-intensive nature of farming, a direct operating model tends to increase volatility in return on assets (ROA).

In contrast to directly operating farms, a leasing model typically provides a more stable and predictable return profile, throughout varied operating profit cycles, thus resulting in a tighter band of return outcomes over the long-term.

How Stagflation Impacts Farmers

Periods of stagflation can put meaningful pressure on primary producers.

1. Sticky Input Costs

Demand for fertilizer, seed, and herbicides, are generally price-inelastic in the short term. Inflationary pressures drive input costs higher without immediately or materially changing planted crop acreage or end demand. Between 2020 and 2025, for example, Canadian agricultural commodity prices have increased by ~10%[3] , while operating costs across Canada have increased by ~41%[4] . This divergence compresses operating margins and can erode profitability for operating farmers.

2. Capital Intensity Risks

In contrast to the sale-leaseback ownership model, direct own-and-operate models are highly capital intensive, traditionally yielding low returns on assets. According to Statistics Canada, from 2020 to 2024, average ROA and ROE were 2.58% and 2.12%[5]. In stagflationary environments, rising costs and stagnant growth worsen these operating returns, forcing operators to rely on leverage which can amplify their financial risk.

These pressures highlight why ownership structure matters, and why returns tied directly to annual operating margins experience significant headwinds in stagflationary environments.

Comparing Ownership Models: Leasing vs. Direct Operating

Direct Operating Model (Own & Operate)

Pros

- ✓ Higher theoretical gross returns, especially during periods of high-crop-prices.
- ✓ Ability to capture more margin through planting and marketing decisions.
- ✓ Control over operating decisions, such as when to plant, spray and harvest.
- ✓ Appreciation of land assets.

Cons

- ! High exposure to commodity price volatility and input cost inflation.
- ! Exposure to operating margin volatility.
- ! Requires significant investment in machinery and non-land assets, which depreciate and reduce long-term capital efficiency.
- ! Annual returns heavily dependent on operating income. Leverage amplifies risk in periods of declining margins and rising rates.
- ! Scale is necessary and can cause concentration risk such as weather and commodity risks.

Practical Implication of the Direct Operating Model in the Current Environment

Current economic conditions demonstrate early signs of stagflation. Commodity prices have risen by approximately 10%[3], while operating costs have surged by 41% between 2020 and 2025[4]. This imbalance compresses margins and erodes profitability. Under these assumptions, our modeled scenario projects an approximate 30% reduction in EBITDA for direct operating models[6]. This projected EBITDA decline reflects only commodity price and input cost fluctuations; it does not factor in geopolitical, FX, and weather-related risks, all of which introduce additional volatility and further erode profitability. This result underscores the heightened risk and volatility inherent in a direct operating model. For many investors, this volatility is misaligned with farmland's intended role as a defensive, stable asset.

Own & Lease (Sale-Leaseback)

Pros

- ✓ Provides stable, contractually defined income independent of annual operating performance.
- ✓ Lease rates can maintain or increase modestly during high-rate environments, with strong demand for quality farmland.
- ✓ Relatively insulated from operational volatility, including input cost inflation, weather risks, and yield variability.
- ✓ Lease agreements can be structured in ways to create reliable cash flow and adequate timelines for remedies if payments are not made on time.
- ✓ Minimal capital investment in depreciating (ie. non-land) assets enhances capital efficiency and focuses return on land appreciation and stable rental income.
- ✓ Low vacancy risk due to deep operator demand and multi-year lease terms.

Cons

- ! Lower theoretical upside when commodity prices spike compared with direct operating.
- ! Less control over land use and cropping strategies. However, this lack of control can be mitigated through the terms of leasing agreements.
- ! Default, delayed payment and vacancy risk if defaults occur early in the year.
- ! Execution risk in land-use change, and capex projects as transitions such as pasture conversion or orchard development are dependent on tenant strengths, such as technical capability, and long-term commitment.

Practical Implication of the Own & Lease Model in the Current Environment

Under Bonnefield's own-and-lease model, rental rates are typically underwritten using a five-year average of commodity prices, accounting for market fluctuations. This approach benchmarks lease rates near the midpoint of farmers' average revenues, ensuring sustainability, predictability, and overall stability of cash flows. This stability significantly reduces exposure to market volatility, as leasing mitigates the impact of input cost swings and commodity price fluctuations that often challenge operating models and is better aligned with investor expectations of low volatility associated with farmland as an asset.

Beyond Economics: Supporting Long-Term Farm Operations

The success of an investment strategy is also rooted in its long-term sustainability. Bonnefield's leasing approach is grounded in supporting the long-term independence and success of Canadian farmers, thus generating ongoing opportunities across the market.

Leasing enables operators to access land without overextending balance sheets and preserving working capital for their core business. This model helps strong operators grow and transition farms between generations, and it maintains local stewardship.

Direct operating models, by contrast, can require operators to sell their businesses, give up or share control over their farming operations, or place undue financial strain should they want to buy back their operations in the future.

The results of Bonnefield's economic analysis underscore the advantages of leasing for investors, while emphasizing the importance of farmers retaining ownership and control of their operations. The own-and-lease model provides long-term access to land and an alternative source of capital, helping farmers maintain operational independence. This approach enables Bonnefield to support strong operators who are looking to grow or transition their farms to the next generation. It tends to support local communities, as individuals who live in these rural areas rely on local business and locally sourced inputs. In contrast, a direct operating model often requires farmers to sell their business and may introduce non-local operators, which can create friction within the community.

What This Means for Farmland Investors

In today's challenging economic landscape, the choice of farmland investment structure is more important than ever. We believe that investors should evaluate risk-adjusted returns and select the investment strategy that optimizes portfolio resilience and capital efficiency under various economic conditions.

Direct operating models may outperform during strong commodity cycles, but they carry meaningful downside risk and volatility when margins compress.

Leasing models can offer greater risk adjusted returns and lower volatility, which is particularly relevant today as stagflation risk increases.

For investors seeking resilient real-asset exposure with predictable cash flow and downside protection, leasing remains a compelling strategy for navigating today's market environment.

---

[1] Statistics Canada: Gross domestic product, income and expenditure. Quarterly Economic and Trade Report. Second quarter 2025. https://international.canada.ca/en/global-affairs/corporate/reports/chief-economist/quarterly/2025-q2

[2] Statistics Canada (Value per acre of farm land and buildings at July 1 - table 32-10-0047-01; Consumer Price Index (CPI) statistics, measures of core inflation and other related statistics - Bank of Canada definitions - table 18-10-0256-01).

[3] Average commodity price increase between 2020 and 2025 for a typical Western Canadian and Eastern Canadian rotation of Canola, Wheat, Barley and Corn, Soybean, Wheat res pectively.

[4] Based on the average input and operating cost increase between 2020 and 2025 for an equally weighted typical Western Canadian crop rotation (Canola, Wheat, Barley) and Eastern Canadian crop rotation (Corn, Soybean, Wheat) as per the 2020 and 2025 OMAFRA "Field Crop Budget" report, and per the 2020 and 2025 Government of Alberta "Cropping Alternatives" report.

[5] Statistics Canada: Balance sheet of the agricultural sector as at December 31st. https://www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=3210005601

[6] Assuming a direct operator with a 50% EBITDA margin, a 10% increase in revenues and 41% increase in costs would result in an EBITDA reduction of approx. 20%. Scenario is illustrative only. Actual results may differ materially.

Bonnefield Financial

Bonnefield is a Canadian agriculture investment manager that provides long-term, non-controlling capital to support farmers and agribusiness operators while targeting stable, risk-adjusted and inflation-resilient returns for investors.

This document is for information purposes only and does not constitute an offer or solicitation to buy or sell any securities in any jurisdiction in which an offer or solicitation is not authorized. Any such offer is made only pursuant to relevant offering documents and subscription agreements. Bonnefield funds (the "Funds") are currently only open to investors who meet certain eligibility requirements. The Funds will not be approved or disapproved by any securities regulatory authority. Prospective investors should rely solely on the Funds' offering documents which outline the risk factors in making a decision to invest. No representations or warranties of any kind are intended or should be inferred with respect to the economic return or the tax consequences from an investment in the Funds. The Funds are intended for sophisticated investors who can accept the risks associated with such an investment including a substantial or complete loss of their investment. This communication is for informational purposes only and should not be relied upon for completeness. Any investment performance data outlined in this document should not be used to predict future returns. Any market prices, data, and third-party information are not warranted as to completeness or accuracy and are subject to change without notice. Prospective investors should take appropriate professional advice before making any investment decision. In all cases where historical performance is presented, note that past performance is not indicative of future results, and should not be relied upon as the basis for making an investment decision. There can be no assurance that any unrealized investments will ultimately be realized at the valuations taken into account in calculating the Funds performance presented herein, where applicable. The performance of such investments when ultimately realized may be materially different. This document may not be transmitted, reproduced, or used in whole or in part for any other purpose, nor may it be disclosed or made available, directly or indirectly, in whole or in part, to any other person without Bonnefield's prior written consent.

Copying, distributing or sharing this document or its contents is expressly prohibited without the express, written consent of Bonnefield. Nothing herein should be construed as investment advice or a recommendation. Suitability must be assessed individually. See our full disclaimer at bonnefield.com/bonnefield-disclaimer/