Influences on Land Valuation Formulation

Research Briefing

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Context

The Scottish Government Rural and Environment Science and Analytical Services (RESAS) division funds the Strategic Research Programme 2022 to 2027 to advance the evidence base in the development of rural affairs, food and environment policies.

One of the themes (Theme E) of the Strategic Research Programme 2022 to 2027 is on Rural Futures. This theme has 3 research topics: rural communities, rural economy and land reform. There are 2 projects within each topic, led by Scotland's Rural College (SRUC) and James Hutton Institute (JHI). This publication sits within a series of publications as part of this theme.

Within the land reform topic, the two projects are

1) Impacts of Land-Based Financial Support Mechanisms on Land Values, Landownership Diversification and Land Use Outcomes
2) Scotland's Land Reform Futures

This current research on land markets and land use change aims to understand whether recent land transactions are leading to (and fuelled by) land use change, for example, towards achieving net zero. Relatedly, it aims to explore the influence of financial support mechanisms on land values, particularly the recent interest in carbon schemes.

It will provide an evidence base for understanding the effects increased land values are having on Scottish Government land reform goals to further improve transparency of land ownership, help ensure large scale land holdings deliver in the public interest, and empower communities by providing more opportunities to own land and have more say in how land in their area is used.

Previous publications are:

A Rapid Evidence Assessment of Investment Decision-Making for Land

Assessing land use change: International evidence review

This research is part of the wider project "Impacts of land-based financial support mechanisms on land values, landownership diversification and land use outcomes" (SRUC-E3-1/C3-1). This Research Briefing sits within a workpackage concerned with Rural Land Values in Scotland. Previous reports in this workpackage include:

Rural Land Values and Land Diversification

Rural Land Values, Sales and Investment Trends

Contents

Report Photos: James Glendinning

Highlights

What were we trying to find out?

Land prices in Scotland took at dramatic upward turn around 2019-21. This was partly due to the interest in natural capital markets, as the Scottish Government introduced ambitious plans for reaching Net Zero and significant financial incentives to pursue Nature Based Solutions to carbon sequestration.

We were interested to find out whether the means in which land values are determined had changed due to this changing landscape.

What did we do?

We interviewed land agents and valuers operating across Scotland and asked about their approaches to valuing land, particularly land with the potential for Nature Based Solutions for carbon sequestration. These expert opinions were collected over two years (November 2022 - February 2023 and December 2023 - February 2024) and in total 38 interviews were conducted (21 in 2022-23, 17 in 2023-24).

What did we learn?

Land agents considered that the general approach to valuing land for agriculture and forestry remained consistent. Nevertheless, the price of land has changed dramatically over the last five years, reflecting changing investment demand and wider market conditions.

A key driver of change has been an increase in demand for land for tree planting, meaning that *plantability* has become a highly significant factor in determining land values, particularly for hill land. Land values have also been influenced by various external market factors notably *interest rates, inflation, timber prices* and *carbon credits* which have impacted investment demand and therefore the value of sales in the market.

The potential to monetise land through *carbon credits* has been another key strand within this picture, creating a new use case for valuation. While carbon was noted as a strong influence on the market, agents commonly took a cautious view on the reliability of carbon price forecasting. The influence of carbon is strongest for hill land and is particularly relevant to the valuation of Scottish Estates. Agents reported that the *plantability* and the *extent of degraded peat* have replaced sporting metrics when assessing the value of upland estates.

What do we recommend and what happens next?

We will continue to monitor developments across the land market and report on changing dynamics. Subsequent briefings are scheduled in 2024.

Executive Summary

Valuing land for Agriculture

- The general approach to agricultural valuation remains the same. The value of arable land is determined by suitability for agricultural production and the strength of demand from local farming businesses.
- Due to strength of demand from the forestry sector in recent years, the value of hill land is increasingly determined by *suitability for tree planting*.
- The period of high *interest rates* and *inflation* following the September 2022 budget has created downward pressure on values in the recent market.
- Some agents considered that there is now less value attached to *farmhouses* due to the growing influence of commercial buyers.
- Similarly there is less demand for *lifestyle units*, which no longer attract as a much of a premium as they once did.

Valuing land for Forestry

- The fundamentals of forestry valuation remain the same, however both the value of forestry properties and of bare land suitable for planting has undergone significant changes in recent years as various factors converged to raise demand for forestry properties.
- A sustained period of *high timber prices* and *low interest* rates supported a positive investment outlook for commercial forestry. Alongside this the emergence of *carbon finance* created new opportunities in woodland carbon investment. Demand from both commercial forestry and carbon investors created upward pressure on the value of land suitable for tree planting, which reached a peak in the 2021 market.
- A subsequent, drop in *timber prices*, increase in *interest rates*, uncertainty and delays to the *forestry approval process*, alongside rule changes at the *Woodland Carbon Code* have dampened the former positive investment outlook, leading to a fall back in the value of standing stock and bare land for planting.

Valuing land for Carbon Investments

- Agents perceived that valuing carbon investments is challenging due to the difficulty of forecasting future *carbon prices*.
- Some buyers pay attention to the specific circumstances in which carbon units are produced. Perceived '*additional benefits*' to water, biodiversity or local communities may have an influence on the price of carbon units, although it is too early to identify the influence of specific factors.

Valuing Scottish Estates

- Estate valuation is complex due to the diversity of potential uses which may necessitate different approaches to assessing value. In order to provide the best advice to clients, agents must continually stay abreast of changing policy, legislation and trends.
- Natural capital has become a key driver of acquisitions in recent years. Due to strength of demand for this use, suitability for developing natural capital investments (*plantability* and *extent of degraded peat*) have replaced sporting metrics when assessing the value of hill land.
- Notwithstanding this, many agents were cautious of using carbon as means of valuing estates, reflecting wider uncertainty around forecasting *carbon prices*.
- More traditional components of estate value such as *amenity* and *residential property* continue to motivate sales and have a significant influence on value.

1 Introduction

Until recently, research on rural land markets in Scotland has been sparse, despite a growing interest in the way that land is used and Scotland having an active land reform agenda. This Research Briefing adds to a body of research that has been growing in recent years which has been commissioned by the Scottish Government and the Scottish Land Commission.

Land prices in Scotland took at dramatic upward turn around 2019-21. This was partly due to the interest in natural capital markets, as the Scottish Government introduced ambitious plans for reaching Net Zero and significant financial incentives to pursue Nature Based Solutions to carbon sequestration. McMorran *et al.* (2022) captured this in their Rural Land Market Insights Report, April 2022 for the Scottish Land Commission. During this time, marginal hill land prices rose from approximately £1,000 per Acre to as high as £5,500 per Acre (Strutt and Parker, 2022). There was somewhat of a 'rush' into Scottish land, as pension funds and other large financial institutions saw large Scottish estates and forestry as a 'safe haven' investment during the financial turbulence and uncertainty caused during and in the aftermath of the coronavirus (COVID-19) pandemic. In parallel to this, the Scottish Government announced generous financial incentives to help steer the Country toward Net Zero, primarily through woodland creation and peatland restoration schemes, with grants available to establish these projects. These schemes would create Carbon Credits through the Woodland Carbon Code (WCC) or Peatland Carbon Code (PCC) which are tradable on an open marketplace or used to 'offset' against a company's carbon balance sheet. Thirdly, the coronavirus (COVID-19) pandemic caused a wave of out-migration from cities to accessible rural areas, which creating upward pressure on house prices and lifestyle properties. This combination of market factors caused the spike in rural land prices.

Researchers have continued to monitor the performance of the land market. In contrast to the booming 2021 market, Merrell *et al.* (2023) reported a greater degree of caution within the 2022 market in the Rural Land Market Insight Report, April 2023. Multiple factors including the war in Ukraine, rising inflation and interest rates, and high commodity prices all contributed to a greater degree of market uncertainty, leading to a fall back in land values. Initial frustrations were also aired concerning the length of time tree planting permissions were taking and changes to the additionality rules of the WCC dimming interest in new woodland creation. The latest edition of the Scottish Land Commission's Rural Land Market series is due in May 2024. This series of reports looked at how the market performed but did not look at *how* values were determined, which is the focus of this Research Briefing.

Additional reporting from the Scottish Land Commission (2023) showed the extent of land transactions between 2020-2022. Utilising Registers of Scotland data, they reported 740 sales of land in this period, and presented results for the farmland,

estates and forestry sectors including total value (£) and total area of sales for each of these over the three years.

In this project, we have previously published two articles on the Scottish land market. Firstly, Rural Land Values and Land Diversification (Merrell *et al.*, 2023) used the first round of interviews to set the stage. At the time, the land agents highlighted the increasing influence of natural capital as a motivator of sales however means of valuing land for natural capital investments were still developing. Our second report Rural Land Values, Sales and Investment Trends (Glendinning *et al.*, 2023), began tracking a range of metrics that appear to be influencing land values, including timber prices, carbon credit prices, marginal hill values and estate values. We used a range of sources, including land agent industry reports to compile this, which was informed by our qualitative enquiry with land agents (reported on in this Research Briefing).

2 Methodology and Data

Qualitative interviews were undertaken with Land Agents and Valuers operating across Scotland. These expert opinions were collected over two years (November 2022 - February 2023 and December 2023 - February 2024) and in total 38 interviews were conducted (21 in 2022-23, 17 in 2023-24).

Land Agents varied according to the size of their coverage (National coverage down to regional/local coverage) and we ensured all sectors of the land market were covered, including interviewing Agents specialising in farmland, forestry and estates. Additionally, some of the larger Agencies now employ staff with expertise around natural capital, which were also included in our sample.

Interviews lasted between 30 minutes and an hour and were conducted over Microsoft Teams by three members of the research team. The same set of questions were asked in each year, but these were semi structured which allowed researchers and agents to explore tangents and emerging points of interest.

Analysis was conducted using Nvivo software. Transcripts were read in full and coded by two researchers to the following codes.

Business Purpose	Valuation Method
Estate	Comparables
Farm	Investment Appraisal
Forestry	
Woodland Carbon	
Peatland Carbon	
Sporting	
Amenity	
Renewable Power	

3 Findings

3.1 Valuing Land for Agriculture

Land agents considered that the **fundamentals of land valuation for agriculture remained the same.** While there was some variation in which factors were emphasised – as captured in the following quotes – the overall perspective was that arable land values are determined primarily by suitability for agricultural production and the strength of demand from the local farming community, with **key factors being; land capability, location, access, field size, topography, and the quality of farm buildings** – where this would enhance the productivity of the farm business.

> *"When you're looking at an arable farm, not much has changed…What does this farm grow, what does it yield and what have similar farms sold for?" (Participant 13)*

> *"I still think that if you're looking for good arable land, you're looking for large size fields. You're looking for good access… good network of infrastructure around it, flat level-ish fields … those things are what people are looking for and that's the sort of land that does command the highest price." (Participant 35)*

"Location and quality of the farm are key. A good size, well maintained model type of farm will of course always command a premium." (Participant 19)

Alongside land capability and the productive characteristics of the farm, **location** has a highly significant influence on value because demand is typically from the local market. The same farm sold in a different region would be expected to reach a different price due to variation in local demand. As the following quote illustrates, some regions are known to have greater buying power than others and good quality farmland in those regions attracts a premium;

> *"The same soil in East Lothian or Angus will be more valuable than it will be in you know Fife, or Stirling-shire, or Kinross-shire because the wealth [and purchasing power] of the arable farming community is greater than it is anywhere else in Scotland … the number of buyers looking for a property in that part of Scotland is greater because it's a well- established farming district with significant farming wealth ready, willing, and able to buy that property." (Participant 34)*

For similar reasons, **land in the region of dairy farms** often achieves higher values because dairy buyers are able to pay significantly higher prices (Participant 14). At a more local scale, the characteristics of **neighbouring farms**, their willingness and ability to expand is also significant. When a neighbouring farm comes up for sale it may be a once-in-a-lifetime opportunity to acquire that piece of land and it may make

sense to pay a premium in order to expand the business or achieve greater economies of scale.

Alongside the characteristics of the land, agents also assess the **quality of farm buildings** with modern buildings attracting a premium;

> *"Anything purpose-built, modern, new, we value more highly than the old traditional buildings which just get in the way I'm afraid of these big arable guys." (Participant 27)*

Modern buildings would also enhance the value of livestock farms, which could enhance the productivity of the farm business and the ability to overwinter cattle.

The value of hill land is increasingly determined by demand from forestry

While factors influencing *arable values* remained similar, a key change that has occurred in recent years has been the dramatic rise in value of marginal hill land. Increased competition for hill land from investors seeking to develop commercial forestry and carbon sequestration schemes has driven up values substantially. Because the typical purchasers of hill ground are increasingly forestry buyers, when a hill farm is brought to market agents will first assess its suitability for forestry – asking *"Is this hill Plantable? Where are the timber transport links?" (Participant 13).* In the words of one valuer – the forestry planting sector has *"moved the goal posts when it comes to demand" (Participant 20 and 21).*

Macroeconomic factors, interest rates and inflation have influenced values in the recent market

The period of **high interest rates and inflation** following the September 2022 budget announcement, were widely considered to have added to market uncertainty including in the farmland sector. The following example concerning a neighbour to neighbour sale further illustrates how increased borrowing costs have led some buyers to re- evaluate and pull out of sales that would otherwise have been expected to go ahead;

> *"So the capital and interest worked out at [£1XX,XXX] a year and he just said, you know, there's no way I can service that repayment [for] 100 acres of extra ground, even with the economies of scale it might generate, so he pulled out of the transaction. I think that's just one small example of the impact of interest rates going from, you know, 0.25% to 5.25%." (Participant 34)*

There is less value attached to farm houses than previously, and a lower premium for lifestyle units

One agent considered that **residential property** was becoming a less significant component of farmland value than it had been in the recent past. When valuing farmland, they would take account of the residential aspect, but this was now a less

significant factor of valuation. There was now less demand for farmhouses due to the increasing influence of commercial growers:

> *"10-20 years ago, it would be a farmer living on the land and the house is probably quite a big aspect of it. Whereas now, especially if you're dealing with a lot of big commercial growers in your area, they just want the land, they don't necessarily want the house." (Participant 27)*

Following the sale of a farm it was common to see residential buildings sold off. Commercial growers did not wish to deal with the inconvenience of property rental and were less inclined to hold on to residential property.

Relatedly they considered that there was now **less demand for lifestyle units**, which no longer achieved the premium that they once had:

> *"There used to be a premium, for small, smaller, attractive sort of, lifestyle units. I'm not convinced that the that lifestyle markets still there. I mean, there are still lifestyle buyers, but I don't think the lifestyle premium is anything like what it used to be." (Participant 27)*

This observation was echoed by another agent who considered that the post-coronavirus (COVID-19) trend for lifestyle purchases of small farms was now receding (Participant 6).

3.2 Valuing Land for Forestry

As with agricultural land valuation, land agents considered that the fundamentals of land valuation for commercial forestry remained consistent. The value of ***land with standing timber stock*** depended on the expected future value of the timber once harvested – **key factors** being expected **timber yield, access, and location relative to market**, while the value of ***bare land for planting*** was assessed based on suitability for growing a timber crop and further depended on **soil fertility**; **altitude** and the **absence of constraints to planting** such as species and habitat restrictions or archaeology.

In either case, forestry investment is forward looking – typical rotation intervals for commercial timber species are 35- 50 years, accordingly the prices that investors are willing to pay also reflect their assessment of the future investment outlook for timber:

> *"When you're planting trees you're not thinking about what's the timber price today. You think about what's the timber price in 30 years time." (Participant 22)*

Most investors are using similar investment models which involve setting out costs and revenues along a timeline to calculate the expected return on investment, and then evaluating the sensitivity of this calculation to changes in **timber prices** and the **cost of borrowing** (Participant 5). Due to this long- time horizon, wider market

influences such as **the policy environment** or anticipated **changes to financial incentives and taxation** that impact on investor confidence over this time- frame may also affect values.

Reflecting the factors described above, one agent described their approach to valuing planting land as an evaluation of site suitability, given the client's intended investment model:

> *"We'll look at all the constraints on the site. We will arrive at a conservative figure for plantability as we call it. And then we will work out how much of that is going to be, which kind of tree… we have to attribute value to all those different areas. And then we will do a sort of investment appraisal on that basis, using a timber price. The assumptions will vary from client to client." (Participant 22)*

Changing Dynamics

While fundamentals of forestry valuation remain similar, both the value of forestry properties and of bare land suitable for planting has undergone significant changes in recent years due to a convergence of factors that have influenced the investment outlook for forestry, and therefore the prices the investors are willing to pay to acquire planting land.

A period of high and rising timber prices supported a positive investment outlook for forestry.

A period of **rising timber prices**, which reached a peak during the resurgence of construction following the easing of coronavirus (COVID-19)restrictions, has been cited as a key factor contributing to increased investor interest in commercial forestry. The **subsequent drop in timber prices** was cited by agents as a key factor contributing to a decline in forestry values since then;

> *"And I think we're in a very different world now the last kind of 18 months… we've seen a significant fall in the value of timber. So standing sale prices are probably anywhere between 25% to 30% down where they would have been 18-24 months ago. And the preceding years before that, they've been steadily rising." (Participant 25)*

While forestry investment is forward looking, and harvest may not be expected for many years, current timber prices influence perceptions of the future market:

> *"Everybody's human and when timber prices are high, people are a bit more optimistic and when timber prices are low, people are a bit more pessimistic." (Participant 22)*

If current timber prices enter directly into investment models then the drop in timber prices will directly lead to a reduction in investment demand. Another agent explained that when providing a valuation the basis for that calculation must be justified to the client. A change in market outlook might be expected to be reflected in

the valuation. This suggests a mechanism through which current timber prices might directly affect valuations:

> *"If you can imagine if you're an agent working for an investor… you have to be able to demonstrate what's your base price… If you were to say, OK, well, let's use last year's pricing at its peak. You're going to be scrutinized on this. People are going to say, well, why do you use that price when the current price is 20% below that? What's to say that it's going to come back?" (Participant 5)*

Due to the long- time horizon of forestry investments, interest rates play a critical role in the decision to invest

Alongside timber prices, **interest rates play a critical role** in forestry investment appraisal. The period of high interest rates following the September 2022 budget was cited as a key factor influencing commercial forestry values. Because interest rates entail the opportunity to lend cash on money markets, where interest rates rise this implies that the threshold rate of return at which investors are willing to commit capital to a long- term investment such as forestry should also increase. The influence of rising interest rates was cited alongside the drop in timber prices as reducing the positive investment outlook that had existed before, leading to a fall back in commercial forestry values (Participant 5, Participant 23, Participant 25).

For a time, investors sought dual investment in timber and carbon, however Commercial Forestry and Woodland Carbon have since been differentiated,

A key influence on forestry values in recent years has been the potential to generate income from **carbon credits**. In response to this opportunity some investors began to develop dual models of timber and carbon investment. However, as described by the following observer, investment has now become more differentiated following a rule change at the Woodland Carbon Code:

> *"The folks who were wanting to be forward thinking and saying, hey, can we get the kind of reliable returns from commercial forestry plus carbon have now seen actually it's very difficult to combine those things after changes in the additionality regulations" (Participant 22)*

Another agent related that one of the larger investors in the market had since lost out following the rule change, because they had bought land based on an investment model that assumed they would receive a certain number of carbon credits, and following the change they would not be able to realise as many (Participant 23). They went on to say that the reduction in investment demand due to the additionality change had led to a considerable drop in planting land values, although this was in conjunction with other factors which were difficult to tease out:

> *"I would say, you know, this 20% drop is effectively the reduction in carbon on new planting land. So that's where that is mainly come out and been born in the pricing. So yeah, you could say that 20% is, it's hard to put a finger on how much of that's the inflation rate, the return on your investment [interest rate rise]*

and carbon, I think collectively it's come in at about 20% reduction in land value. But primarily on schemes that would have a higher percentage of conifer" (Participant 23)

More generally, the additionality change was referred to by multiple agents as a factor that led to a "cooling" of forestry investment (Participant 10, Participant 30, Participant 36).

Uncertainty around planting permission was cited as a key factor influencing both investment appraisal and land values

While there is significant political support for tree planting in Scotland, land agents working in the forestry sector perceived that the approvals process for woodland planting is a barrier to investment. Agents reported lengthy delays and **uncertainty around the time taken** to achieve planting permission, as well as uncertainty around **what level of planting** can be achieved and **what species mix** would be permitted. Agents perceived that the effect of uncertainty was to create additional risk, and ultimately reduce the number of investments that go ahead:

"Approvals is a significant barrier… I think it really brings about huge uncertainty…. We can look at a piece of land and say silviculturally that this has a lot of opportunity but actually we can't get any certainty out of the regulator as to what we might be able to achieve… We've seen sites that 30 years ago you would have planted wall to wall with trees and we have just let them go. We've just walked past them because we have no certainty about what we could achieve" (Participant 25)

The **proportion of productive timber species** that can be planted is critical to the future profitability of commercial forestry investment. Some agents perceived that there was pressure within the approvals process to reduce the proportion of conifer species. As the following quotes illustrate, the uncertainty that this creates has a direct influence on investment appraisal and through this land values:

"People were basing their land value on what they could make in the way of timber… What proportion of the area you could plant with conifer… In the past you maybe got 75% conifer now you're being pushed down, down, down, and you know some conservators are wanting 50 50, which is absolutely ludicrous. So that can only do one thing but reduce the value of the land…I'm seeing land prices coming down for certain areas where people are thinking, OK, if I can't get certainty from Scottish Forestry that I can plant this, I'm going to build in an element of risk value into this this." (Participant 5)

3.3 Valuing Land for Carbon Investment

The potential to access carbon credits through the Woodland Carbon Code and Peatland Carbon Code has provided a new use case for valuing land.

Woodland Carbon Units are awarded for carbon sequestered during tree growth. The number of units that may be expected depends on factors that influence tree growth such as **soil fertility, altitude** and the **absence of constraints to planting**. ***Peatland Carbon Units*** meanwhile are awarded for improving the condition of degraded peat and preventing emissions that would otherwise have occurred. The number of units that can be expected depends on the **extent and condition of degraded peat** that may be restored.

To provide an accurate valuation requires a feasibility study to assess site suitability. Without this it may be possible to provide an indicative range of values, however, this would require significant assumptions (Participant 20 and 21, Participant 12). Input from a range different specialists may be required, with some agents having access to this expertise in-house whereas others contract this work out.

Pricing Carbon is challenging and open to risk

The potential return on investment for woodland and peatland carbon investment depends critically on forecasted carbon prices. While the recent increase in value of hill ground values strongly suggests that purchasers have placed a significant value on carbon, land agents offered a range of views on the **reliability of carbon price forecasting**. Commonly agents perceived carbon pricing as somewhat speculative or open to risk in the current stage of market development:

> *"Theoretically you could plant this area and … [it will yield] this many carbon units, but because it's an emerging market, it's very difficult to put a figure on what the value of that that natural capital will be to any given investor… [it's] very difficult and I think prone to quite a lot of risk." (Participant 26)*

> *"All these figures are based on projections of what carbon is going to be priced at in 30, 40, 50 years' time, so it's speculation I think, or an educated guess." (Participant 28)*

> *"That price per ton is very much up for discussion" (Participant 20 and 21)*

Offering a contrasting perspective on the reliability of future carbon values one agent considered that the recent data on prices in the market published by the WCC had given more **confidence in carbon values**:

> *"Some really great data was published recently by the Woodland Carbon Code… it's broadly doing what we thought it was going to do… when I joined*

[Agency], we were talking about a woodland PIU being £25 and now that's being confirmed... So that was a nice kind of confidence boost." (Participant 29)

'Additional benefits' have an influence on price

The Land Carbon Registry provides a platform through which buyers and sellers can communicate. Transactions are somewhat bespoke and are conducted through negotiation between buyer and seller (Participant 29). When it comes to pricing, not all carbon units are the same. It was highlighted that some buyers increasingly pay attention to the specific circumstances of particular projects. Certain types of buyer attach an additional value to *"charismatic carbon"* that enables them *"to tell a good story"* about how their emissions have been offset (Participant 26) or point toward *"additional benefits"* to biodiversity, water or local communities:

"If you can measure the biodiversity benefit… or it's got social value or it's got a particular brand associated with it, like it's in a National Park, you know, that kind of thing would be worth more" (Participant 29)

In the current stage of market development there doesn't seem to be enough evidence to *"drill down"* and tease out the relative influence of particular additional benefits (Participant 26), however it was suggested that some types of buyers (e.g. a University) may be more attuned to additional benefits than others (Participant 29).

3.4 Valuing Scottish Estates

Scottish estates range in size from a few hundred to tens of thousands of hectares and occupy a wide range of land classifications, often within the same property. At the smaller end of the scale it may difficult to distinguish an estate from a diversified farm business. At the other end, some Highland estates extend for tens of thousands of hectares and may further include a significant number of residential and commercial properties. Reflecting this diversity, Scottish estates support a wide range of business (and non- business) use cases. Alongside agricultural holdings, estate businesses often include forestry, renewable energy, tourism, residential property, stalking and shooting (Hindle et al., 2014).

For some time, Scottish estates have been sought as discretionary purchase by wealthy individuals, potentially combining various motivations such as amenity, sporting, rural development, and more recently natural capital motivations. Due to this range of use cases and factors influencing demand, estates are challenging to value and land agents highlighted that valuation requires a keeping abreast of market trends (Participant 22).

A common approach to estate valuation is to assess and value the different components (Participant 10, Participant 18, Participant 20 and 21). Following this approach the agricultural component would be valued as a farm business, the

residential component separately valued and any additional businesses valued on their merits.

Suitability for developing natural capital investments has replaced sporting metrics when assessing the value of hill land

Many Scottish estates comprise large areas of hill land, that have traditionally been of low value due to having constrained potential for agriculture. Within estate valuations, hill land was traditionally afforded little value (by area), except where this enabled stalking or shooting in which case sporting metrics – bags of grouse and head of deer shot – typically averaged over the last five to ten years, would be applied in order to derive a capital value for sporting interest.

As has now been widely reported, natural capital has become a key motivator of estate purchases due to natural capital investors seeking land in order to access woodland carbon and peatland carbon credits:

> *"For these big inflated prices, key drivers of interest are extent of peat and extent of land suitable for planting" (Participant 1)*

Accordingly, the potential to develop natural capital investments has brought new means of assessing the value of marginal hill land. As related by two specialist valuers, the potential for tree planting and peatland restoration is now the first use case applied to assess the value of hill land because this now reflects "highest component of value" (Participant 20 and 21). Where tree planting is feasible, the value under this use would typically exceed the grazing value, or value of sporting interest (Participant 20 and 21).

Several agents were cautious of using carbon as means of valuing estates

While the **potential to access carbon credits** was highlighted as a key driver of estate purchases (and by implication how the purchasers had assessed value) several agents expressed a cautious view around valuing estates for carbon investments. One highlighted that their agency did not place a high value on carbon when advising clients, particularly if this was in support of a bank lending decision:

> *"Certainly the value for the banks or one of the lending institutions, we wouldn't really put a great deal of value on carbon… as a firm, we're probably more cautious in valuing carbon than other firms might be" (Participant 27)*

Reflecting on the estates market as a whole, an agent specialising in natural capital and estate sales considered that **investors in the market** were now more cautious of carbon pricing:

> *"I think there is probably a pause or a sort of a caution if you like around the modelling on which the prices are based… my sense is that [while] the appetite*

is there, there's a caution around the approach to the valuation model." (Participant 32)

Traditional factors such as amenity and residential property continue to enhance values

Amenity purchases by wealthy individuals continue to be a significant feature of the market (Participant 1, Participant 27, Participant 31). **Visually attractive features** such as coastline, river or loch frontages, as well as the ability to offer an exclusive location all add to the desirability and amenity value of properties (Participant 1). Alongside this, one agent considered that there continues to be a good market for *"good quality"* residential property that is attractive to high net worth individuals:

> *"Overseas money, South of England money, there is a lot of money sloshing around to buy big rural property… But it has to be good quality, well maintained and accessible." (Participant 27)*

Estate valuation is complex and different use cases may necessitate different approaches to assessing value

Given the diverse range of potential use cases that exist estate valuation can be a complex task. An agent performing a valuation (whether acting for buyer or seller) requires a good understanding of potential buyers motivations because this then influences how value may best be assessed:

> *"A mixed upland estate… If it's priced attractively you might have three or four or five offers at a closing date from different individuals that have totally different intended future uses. From the point of view of a valuer… [it makes it] quite an interesting challenge because part of it is understanding what the buyer wants to get out of it and then understanding how to assess value in that way." (Participant 32)*

Accordingly, for valuers operating within this environment it is critical to stay alert of trends in policy and legislation that may affect how *"purchasers see that land and how they interpret value." (Participant 22).*

Conclusion

Drawing on interviews with land agents in Scotland over two years this briefing has sought to understand how land values are determined and whether this is changing due to net zero policy commitments and related financial support mechanisms targeting Nature Based Solutions to carbon sequestration.

Land agents pointed to a complex picture. In the first instance, differences in land values reflect differences in suitability for developing land- based businesses. In this sense, the factors that determine suitability for agriculture and forestry have remained consistent. The best quality arable land in the best regions continues to attract the highest prices.

Nonetheless, land prices have increased dramatically in the last five years, particularly for hill land and for upland estates suitable for tree planting or peatland restoration. Land agents pointed to a complex set of factors in the wider market; notably interest rates, inflation, timber prices and carbon credits which have influenced the investment outlook, contributing to a boom and subsequent falling back in forestry values and the value of land suitable for tree planting.

Opportunities provided by carbon and natural capital markets have been a key driver within this. The potential to access carbon credits contributed to the increase in demand for plantable land and the rapid increase in land values. For a time, some investors pursued dual models of timber and carbon investment. A subsequent change in the additionality rule at the Woodland Carbon Code however has made it harder for commercial forestry investors to access carbon credits (unless they opt to forgo grant funding). Land agents considered that the rule change contributed to the cooling of forestry investment and the subsequent falling back in land values.

Carbon credits have created a new use case for valuing hill land. Land agents reported that suitability for developing natural capital investments has replaced sporting metrics when assessing the value of upland estates. Despite this many agents expressed a cautious view of valuing land based on forecast carbon values.

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Appendix 1. Interview Schedule for Focus Group with Land Valuers 2022/23

Which sectors do you (personally) work in?

How are land values performing since last year? Are they largely up or down?

What current factors are of greatest importance in influencing values?

Que: Size, location, topography, amenity value, access, sporting, natural capital values, asset base/income potential, land use and land use potential (including increased focus on food security), running costs, development controls

Are these factors changing over time? Which are more relevant and which are less relevant?

How useful are (traditional) comparables in this new market? Are you developing new comparables relating to natural capital?

Are there particular types of land (farm/estate/forestry) that you have noticed where comparables are drastically changing? Are there significant changes in value as well?

Farm land – Prime arable land, mixed farms (potentially diversified), marginal/upland

Estates – Peatland restoration, sporting, renewables potential

Forest – Commercial forestry, afforestation (native broadleaves) for natural capital payments

How much of a driver or barrier are current government policies and grants around natural capital?

Probe: different types of natural capital forestry, commercial forestry, peatland, and wider natural capital (carbon, biodiversity credits, flood water retention, renewables), planning permission for forestry, planting regulations, inset/offset debate

How do you see values changing in the future? What are your reasons for this?

Appendix 2. Interview Schedule for Interviews with Land Agents 2022/23 and 2023/24

Current trends in the market

How is the land market performing since last year? Is it largely up or down?

What does the supply against demand look like?

What is the amount of off market activity compared to on market?

Are there particular types of land (farm/estate/forestry) that you have noticed a significant change in?

Probe individual types:

Farm land – is it smaller or larger farms that have experienced changes? Are farms being broken into lots and are these being bought as lots or package? Are people buying farms to farm on, or run other businesses? **What is the amount of off market activity compared to on market?**

Estates – is it smaller or larger estates coming on the market? Are they above or below market value? **What is the amount of off market activity compared to on market?** Splitting of estates (small parcels or splitting into lots)? Succession?

Forest – Are forests being sold or is it bare land for planting? **What is the amount of off market activity compared to on market?** Are sales relating to commercial forestry or afforestation/rewilding?

Are current subsidies and/or agricultural support affecting the market?

How much of a driver or barrier are current government policies and grants around natural capital?

Valuing Land

What current factors are of greatest importance in influencing values? (Size, location, topography, amenity value, access, sporting, natural capital values, asset base/income potential, land use and land use potential (including increased focus on food security), running costs, development controls)

Do you account for natural capital potential when valuing land? How about the cost of carbon?

Are there any new factors emerging? Are any factors becoming less relevant?

Current primary motivations/drivers for selling rural land (Upsizing, death, debt/bankruptcy, divorce, family reasons, profit taking, lifestyle change, relocation, retiring, downsizing, unknown, CGT rollover, IHT benefits, neighbouring land, long-term development, land use change restructuring)

Are there any new patterns arising in terms of motivations?

Are you noticing any institutional investors/corporations deciding to enter the market or sell?

Current primary <u>motivations/drivers for purchasing rural land</u>

What are the main types of buyers you have seen this year? Where is demand coming from?

What are **the motivations** of new entrants?

> What proportion of new owners have a natural capital related motivation and can you expand on this in terms of effects on sales/acquisitions? (scale, type of activity etc.)

To what extent are new acquisitions/changes in ownership resulting in a substantive change in land use (e.g. farm-forestry conversion etc.)

Forecasting

How do you see the market changing in the future? What are your reasons for this?

Are there any future threats or challenges you foresee?

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