Landowner Ecological Asset Value - Ten Lessons Learned

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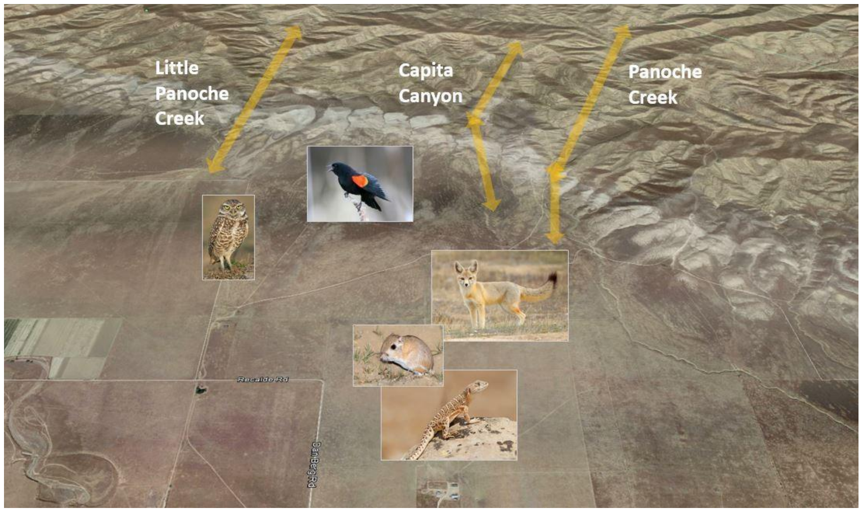
EASI recently updated its Land Value Slide Deck for 2019. What emerged was a set of ten lessons learned that every rural landowner should see. These lessons come from case studies in ecological asset valuation, mitigation bank development, and land appraisals completed over the past five years. These highly practical results highlight the importance of including eco-asset values in any land planning exercise, especially rural land development and appraisals. The bottom line message is this: ranchers (and farmers) should consider these lessons as a way to optimize annual earnings and land valuation. These lessons also support future land sales and estate planning efforts.

Lesson 1 – Ecological assets in the form of wetlands, species and water quality credits can generate significant one-time revenues for (happy) landowners.

This lesson has been proven hundreds of times over the past thirty years as the market for mitigation credits has grown and diversified. We know that mitigation bankers now hold (round numbers) $300 *billion* in market-ready eco-assets nationwide. How do we know? EASI has carefully tracked the economic value of wetland credits, stream credits, species and habitat credits – land based ecological assets. We have tallied the number of credits that have been approved by federal agencies. Multiplying the average price paid for these credits times the number of approved credits allows us to derive a reasonable estimate of nationwide asset value for the mitigation banking industry as a whole. The industry has created $300 billion in commercial paper assets and enjoys about $4.8 billion in annual credit sales. Not only that, but the industry has dedicated more than 2.5 million ares to long term conservation tied to mitigation banks. These trends will continue as agencies diversify and expand policies supporting environmental compliance via compensatory mitigation.

Lesson 2 – Just knowing a property's *potential* ecological asset value can boost land sales.

Many landowners have heard that creating a mitigation bank can be time consuming and expensive. They've heard that mitigation banking is a business unto itself, with its own language and rules of the road. This makes them cautious about digging into the details of land ecological asset valuation since mitigation banking seems far removed from the core business of farming and ranching. But it turns out that creating a mitigation bank isn't always necessary in order for a landowner to benefit from the presence of ecological assets – wetlands, riparian zones or habitat for rare species. Buyers may agree to premium prices for eco-asset rich parcels, especially if outside pressures such as regulatory compliance have increased their willingness-to-pay. This means that landowners should inventory potential eco-assets, stay abreast of current market prices, and look for opportunities to leverage that land value as new development projects are announced.

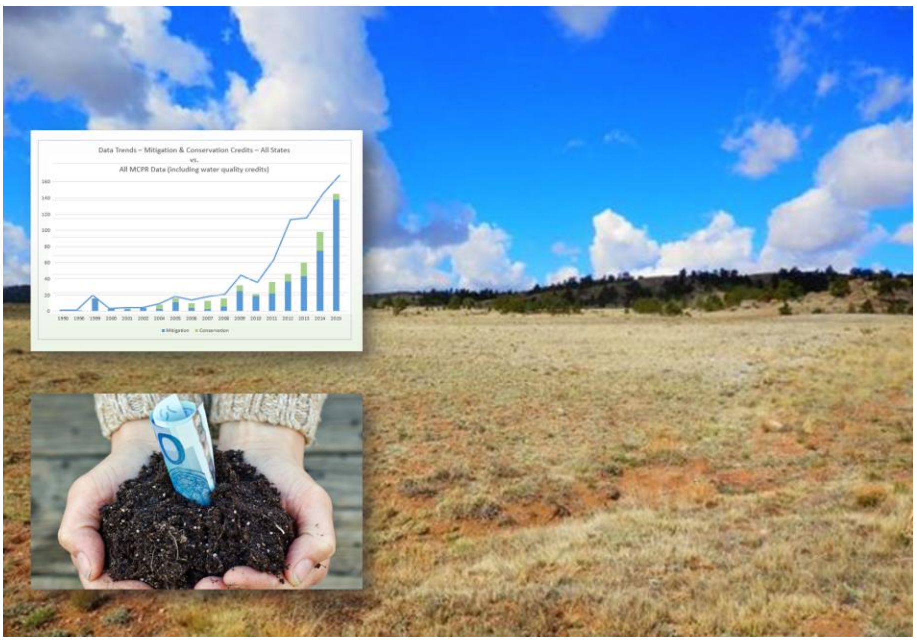


Lesson 3 – Eco-assets can increase the *gift value* of land, and the related tax value of that gift. This is also true when figuring estate value and personal net worth.

Donating conservation-rich lands to non-profits or government entities has long been seen as a way to earn tax credits and reduce tax liabilities. But land value depends on more than just traditional uses for agriculture or animal husbandry. It depends on more than the value of traditional land based commodities such as water, minerals or oil and gas. Ecological assets, and the market value of potential mitigation credits, should also be part of the land appraisal equation. This can boost the worth of land and consequently improve the downstream benefits of tax deductible gifts and/or overall estimates of net worth.

Lesson 4 – Mitigation credits, although intangible assets, have known market value. That value can be leveraged to support debt financing.

Lenders have recently learned that mitigation credits have real market power. The credits have a 30-year history and a proven track record especially in high growth areas. Mitigation credits are anchored to the land and track with changing land ownership. Borrowers have been successful showing that mitigation credits qualify as collateral in the same way that traditional assets like minerals, water or oil and gas can do.

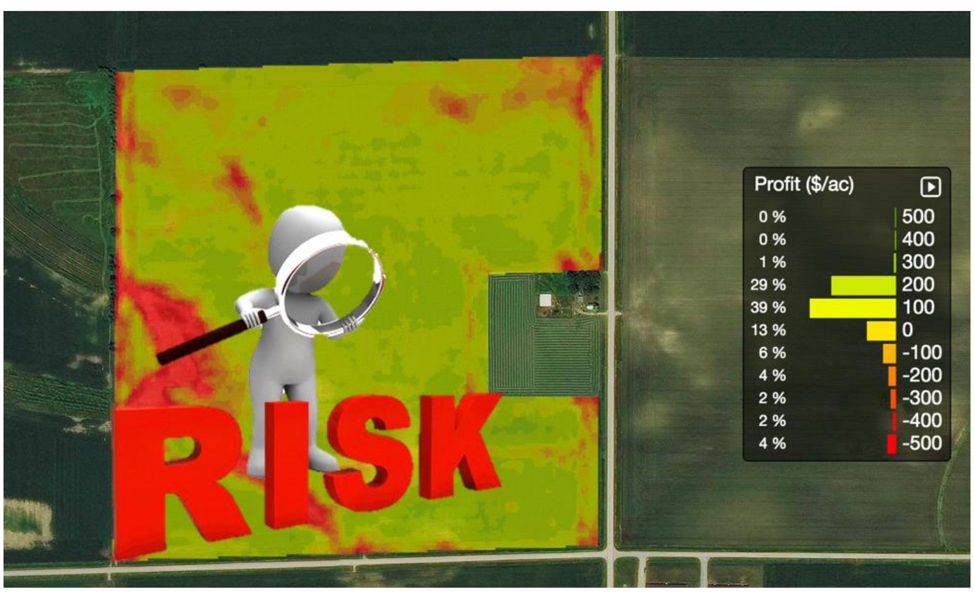


Lesson 5 – Figuring out the gross or bulk eco-asset value of a property is only the beginning of a successful mitigation bank venture. Development costs and market conditions are equally important determinants of long term mitigation bank success.

Mitigation banking is full-on business undertaking with its own specialized requirements. A new mitigation bank demands comprehensive analysis beyond predictions of potential gross revenues. Learning about development costs (which vary region to region) helps to determine simple benefits-to-costs ratios. But market conditions such as mitigation credit supply vs. demand, and predicted sales timelines should also be studied to fully understand predicted net present value (NPV) or return on investment (ROI).

Lesson 6 – Just like any business undertaking, mitigation credits don't always generate desired profits.

After all the data comes in sometimes the NPV/ROI numbers work to the landowner's favor, other times they don't. Either way, a careful business analysis is called for in any land development undertaking, including mitigation banking. This is the only way to manage business risk, increase the confidence of business decision making and improve opportunities for success.

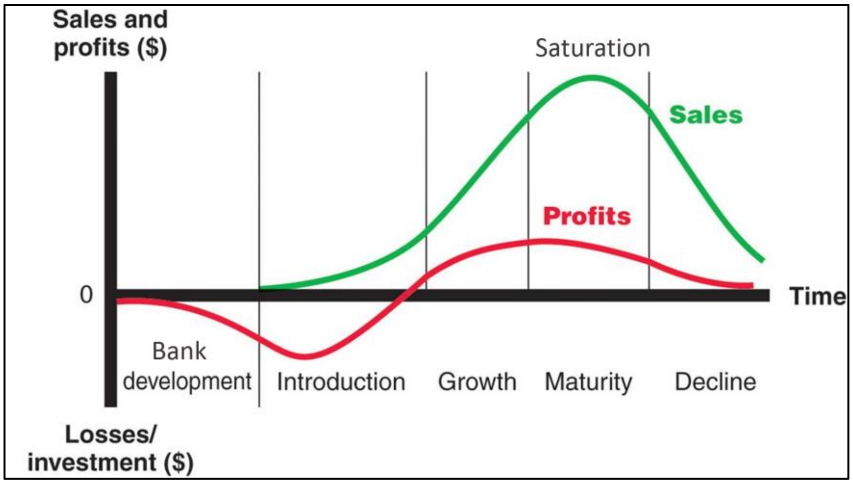


Lesson 7 – Attractive potential earnings are not always the determining factor in mitigation bank development decisions.

Landowners know that development decisions are not always based on the business bottom line. Other factors such as landowner personal preferences and priorities can unexpectedly come into play. Mitigation banking is no different, even when a strong return-on-investment has come to light. Planners should always be prepared to postpone or even walk away from a seemingly high-value opportunity if landowner attitudes change.

Lesson 8 – Market saturation can be problematic in some areas, making it difficult for promising new mitigation banks to be successful.

A property may have all the characteristics of a successful new mitigation bank: ecological assets may be abundant, development costs may seem reasonable, and mitigation credit sale prices may look attractive. But if too many credits have been brought to market by competing mitigation banks, and if local demand for credits is not growing, the market may have become saturated. A careful business analysis is always called for -- to include a thorough examination of mitigation credit supply vs. demand.



Lesson 9 – Hard market value is not everything for ecological assets. 'Soft' eco-asset value can build willingness-to-pay for an attractive property, especially if promoted by a reputable party.

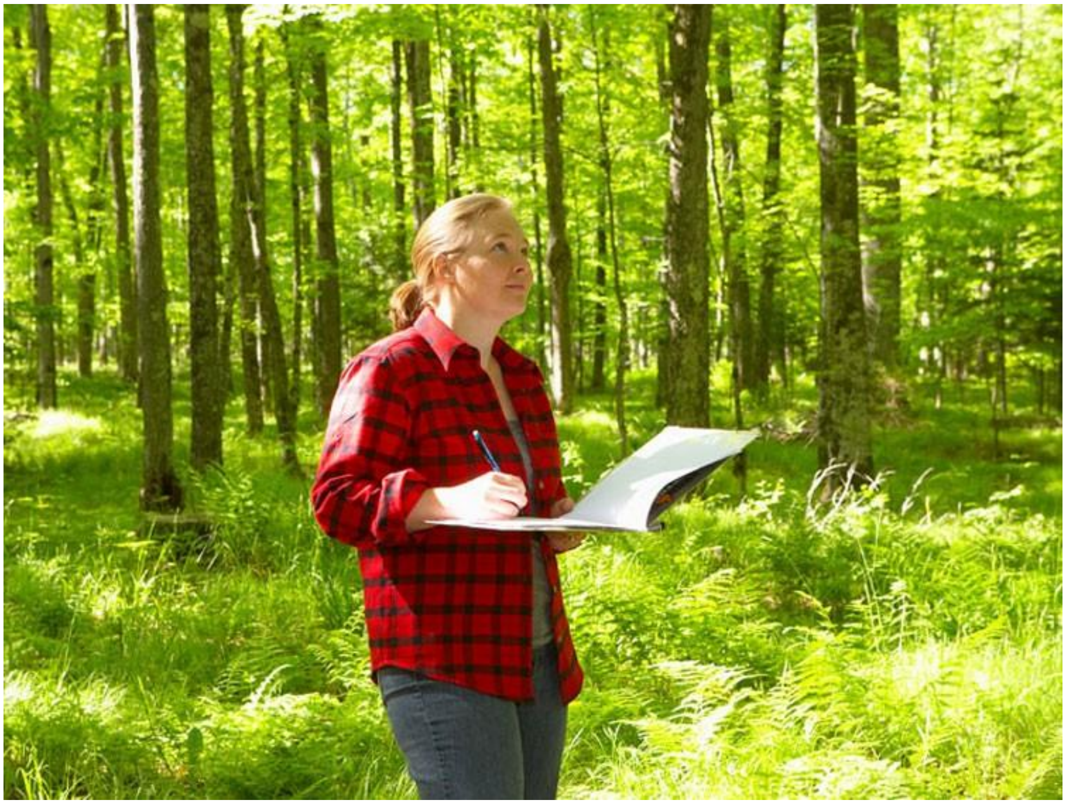
Prices for mitigation credits shed light on direct or 'hard' market value of local ecological assets. But this is not always representative of a landscape's total economic value. Indirect market values such as recreation, or long term existence and bequest values may be equally important to buyers. These subjective considerations can resist definitive estimation. How can personal opinions about land value be converted to something conclusive? By drawing on the opinions of reputable specialists who are skilled in data gathering and analysis methods supporting 'soft' market valuations. Trustworthy views about such indirect values may help boost buyers' willingness to pay.

Lesson 10 – Knowledgeable buyers will underbid eco-asset rich properties knowing they can be flipped.

It goes without saying that sellers are looking to maximize gain while buyers are looking for a bargain. People who are knowledgeable about ecological assets may happily pay traditional appraised value for land when they know it carries untapped commodities capable of earning a handsome profit. Mitigation credits are an example. For all the strength and rapid growth of the mitigation banking industry, only a tiny fraction of properties have been inventoried for their eco-asset market potential. Plus the market for eco-assets is constantly changing; new asset development prospects may present themselves at any time. Smart land shoppers will hunt for opportunities to 'buy low and sell high', to 'flip' a land investment and take home strong earnings. Landowners deserve to be well informed about all aspects of property value including the ecological assets that are part of the natural landscape.

Wrapping It Up

Ecological assets – in the form of potential mitigation credits – are the invisible factor when it comes to tallying land value today. Lack of knowledge about eco-asset values can place the landowner at a disadvantage. As a partial remedy to this problem, the ten lessons presented here should be part of every landowner's checklist when it comes to estate planning, estimating potential land revenues, or positioning a property to sell. Once the lessons have been learned, the landowner should look for resources to assist with eco-asset valuation, mitigation bank business analysis and, ultimately, eco-asset development and market pricing.



For more information about the case studies described here, see the EASI 2019 Land Value Slide Deck available at www.easillc.com. Or contact EASI directly at info@easillc.com, 415-706-6154.

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