savills

Savills World Research
UK Rural

Scottish Estate Benchmarking
2013 Survey

January 2014

This publication
This document was published in January 2014. The data used in the charts and tables is the latest available at the time of going to press. Sources are included for all the charts. We have used a standard set of notes and abbreviations throughout the document.

Estate structure
Within the survey, the average estate structure for 'All Estates' is just under 8,000 acres of lowland area, including about 80 residential properties and commercial and leisure enterprises.

Estate ownership
Institutionally owned estates represent around 25% of the estates in the survey with the remainder in private ownership. The owner is resident on about half of the privately owned estates.

Ownership objectives
Long- term retention of the core estate and income generation remain the key objectives for the owners of rural estates followed by return on capital and environmental stewardship.

Footnotes
We regularly review our survey data which means the data published each year may not exactly match that published in the previous year's survey. Separate results are published for English estates.

Scottish Estate Benchmarking
2013 SURVEY

Strong results have been posted in 2013 for Scottish estates, with an improving outlook extending across all estate assets

Savills Estate Benchmarking survey demonstrates that Scottish estates have posted strong results in 2013. The glimmers of light being seen within the wider economy have had a positive impact on the rural sector. Indeed, there was a 33% uplift in gross income, with the improving outlook extending across all estate assets.

This has been achieved against a challenging backdrop of uncertainty brought about by the forthcoming Land Reform and Agricultural Holdings Acts review and the impending Independence Referendum in September 2014.

The results demonstrate how rural communities are benefitting from increased returns, as estates continue to reinvest higher proportions of their improving incomes into local economies in various ways. Estates continue to provide high quality affordable housing stock in the shape of pensioners accommodation, tied properties and family homes at below open market rents.

In addition, landowners have been able to increase their expenditure on improving the quality of their let agricultural and residential buildings for the benefit of tenants. Finally the sums spent on community and environmental projects have risen. From river bank repairs, improved public access, wildlife management and biodiversity schemes and renewable projects, the Scottish estates sector has proved more than ever this year that they have a key role to play in the responsible stewardship of the Scottish countryside.

Our estate benchmarking survey results reinforce the benefits of maintaining an involvement in different assets and enterprises in order to secure a stable income stream, while realising capital growth.

The results demonstrate that despite the significant growth in returns from traditional agricultural and residential sectors, alternative uses are playing a greater part in the economics of estate businesses. Increased diversification will inevitably assist estates overcome volatility peaks, such as those suffered in years of exceptional weather and poor harvests.

In addition, estates will continue to develop renewable energy projects harnessing natural resources and contributing to meet European and worldwide carbon emission targets.

Estates continue to invest large sums to improve let agricultural and residential properties. There are challenges ahead with potential changes to legislation which may increase bureaucracy and the ability to deliver quick solutions. Additional challenges include forthcoming changes to Energy Performance Certificates which may require significant capital improvements to let residential portfolios.

Landowners continue to demonstrate their willingness to plough back profits into their local areas. This, combined with the increasing optimism in the economy, should bode well for Scottish estates. However, there is real concern over land reform and the independence referendum which could constrain landowner's ability to continue to invest such large sums. Proactive management to mitigate against the potential risks will be imperative.

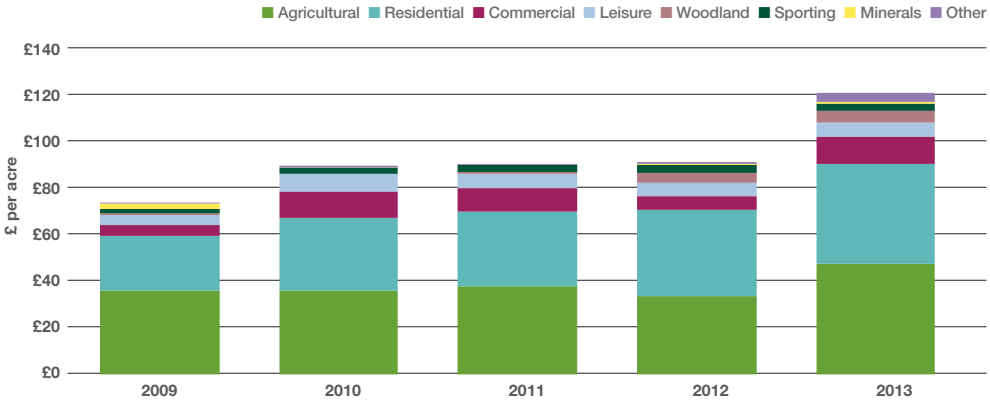
> "The glimmers of light being seen within the wider economy have had a positive impact on the rural sector"
> Savills Research

Kenneth Munn
Head of Scottish Benchmarking
+44 (0)141 222 5870
kmunn@savills.com

Estate Benchmarking
INCOME

GRAPH 1

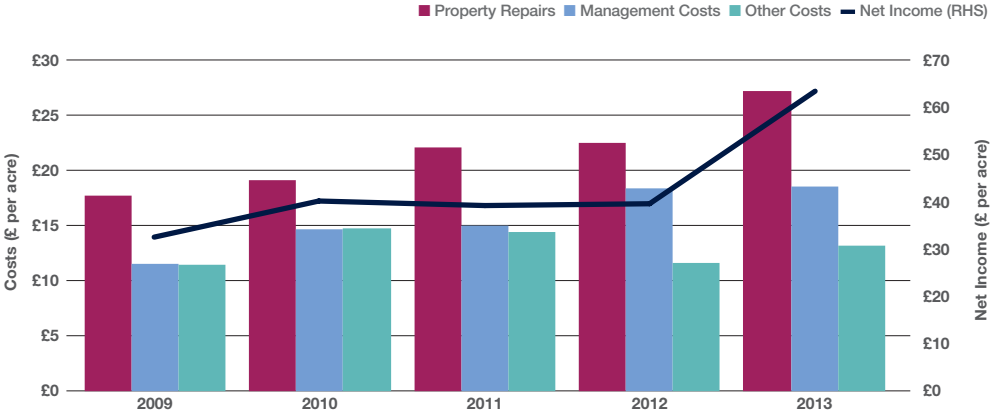
Source of income



Source: Savills Research

GRAPH 2

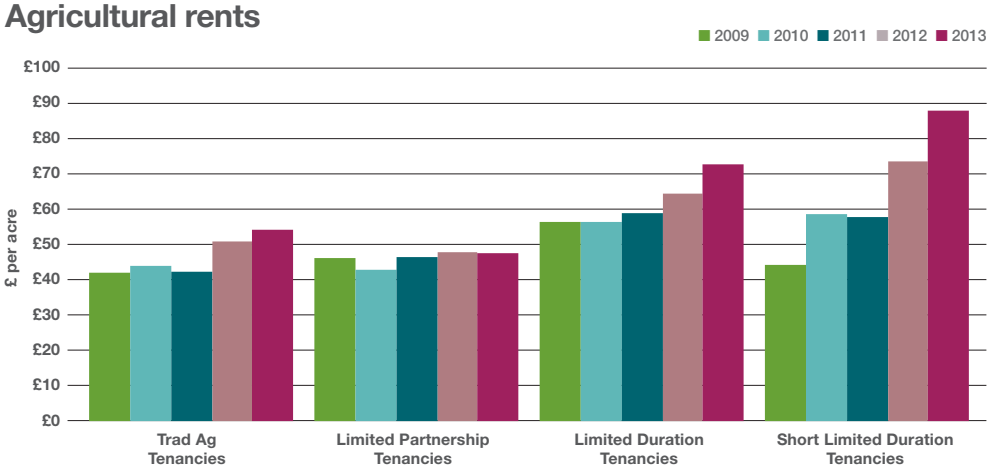
Net income and expenditure



Source: Savills Research

GRAPH 3

Agricultural rents



Source: Savills Research

The 2013 survey results show that average gross income on 'All Estates' in Scotland increased 33% to £123 per acre (£304 per ha) across the whole estate (including woodland). Annualised growth over the past three years was 11%. Income rose across most of the key sectors but especially so for the commercial sector where renewed economic confidence appears to have played a part.

Although costs increased 12.3% during 2013 to £59 per acre (£146 per ha) it was at a much slower pace than gross income which resulted in a substantial 60% increase in net incomes (before depreciation, finance, drawings and tax) to £64 per acre (£158 per ha).

Graph 1 illustrates the change in proportion of income derived from the key sources on rural estates over the past five years.

Agriculture

Agriculture remains the main income source on rural estates, and in 2013, contributed 39% of gross income or £48 per acre (£119 per ha).However, the increased income generated from the residential and commercial/leisure sectors has reduced agriculture's overall proportional contribution to 39% in 2013 from almost 50% in 2009. This contrasts to England where residential now contributes a higher proportion of gross income.

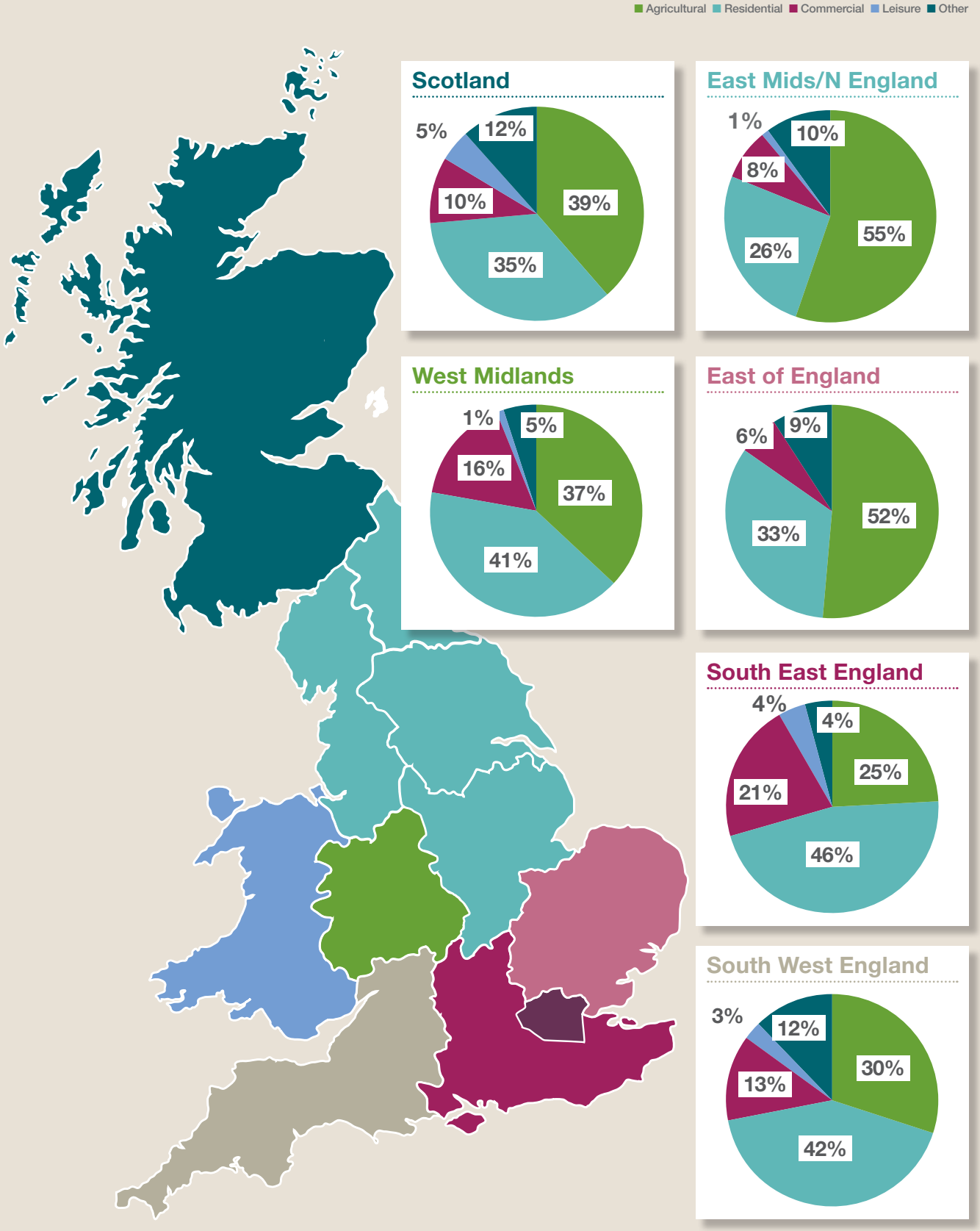
Looking specifically at the let area of the average estate, income from all let agricultural sources in 2013 increased by 13.5% to £60 per acre – mainly driven by LDT and SLDT growth.

Due to the difficult harvest in 2012, in hand farm incomes (after deduction of property repairs, insurance, third party rents and interest on borrowed working capital) on 'All Estates' fell by -22% to £13 per acre in 2013.

We expect pressure on in hand operations to continue as the additional costs of redrilling 2013 harvest winter crops with spring crops takes its toll on cash flows into the 2014 harvest year. However, the pressure has been softened by a good autumn enabling the majority of 2014 harvest crops to be planted.

MAP 1

Proportion of income by region for 2013



Source: Savills Research

➔ Our survey records average agricultural rents in 2013:

- **Traditional Tenancy:** £54 per acre (£133 per ha), up 6.5% on 2012.
- **Limited Partnership Tenancy (LPT):** £47 per acre (£116 per ha), similar to 2012.
- **Limited Duration Tenancy (LDT):** £72 per acre (£178 per ha), up 13.1% on 2012.
- **Short Limited Duration Tenancy (SLDT):** £88 per acre (£217 per ha), up 19.6% on 2012.

Traditional agricultural tenancy rents continue to increase with an annualised increase of 6.5% to an average rent of £54 per acre, up almost 29% since 2009.

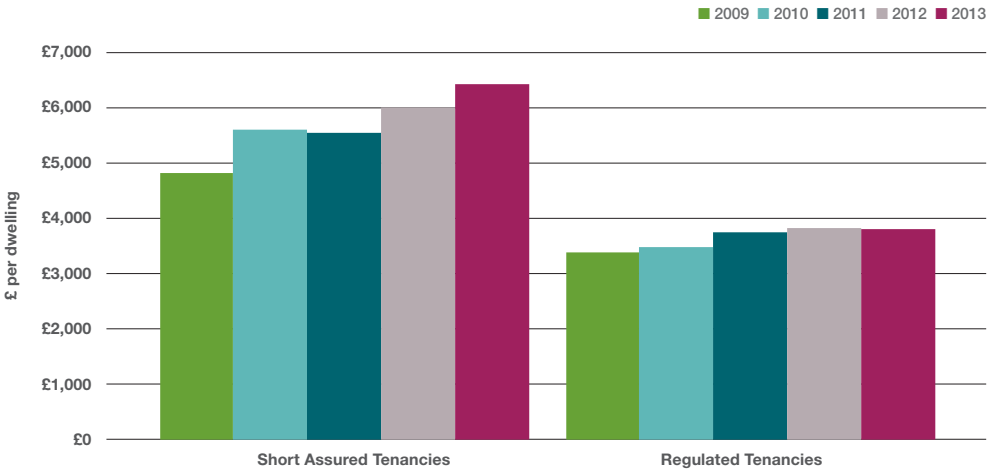
Residential

Average income from residential sources on 'All Estates' increased in 2013 by 15% to £42 per acre (£104 per ha) and represented 35% of gross income. This growth is a combination of rental increases and a significant rise in the proportion of Short Assured Tenancies (SATs); 52% of all properties in 2013 compared with 46% in 2012.

Our survey also recorded a fall in the proportion of residential properties tied up in agricultural tenancies or in hand operations from 40% in 2012 to 34% in 2013.
Average annual rental income of SATs on 'All Estates' increased by 7% during 2013 to £6,468 per dwelling.

GRAPH 4

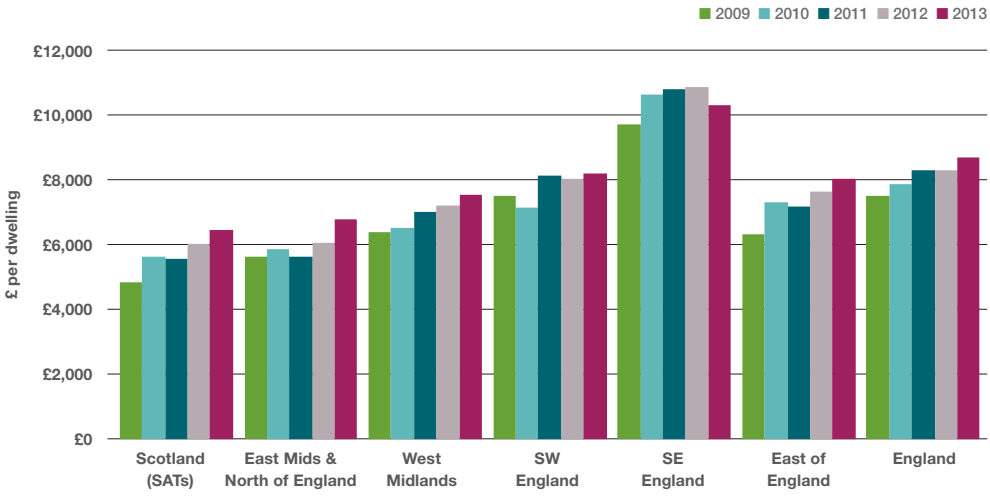
Residential Rents



Source: Savills Research

GRAPH 5

Regional Residential Rents



Source: Savills Research

In England average market (ASTs) increased in 2013 by 4.6% (to £8,723 per dwelling).

Location affects residential rental levels and this can be illustrated using regional English data. The South East of England recorded the highest average AST rents at almost £10,500 per dwelling (see Graph 5).

However, there was evidence of pressure at the top end of the rental market with the South East recording a -5% fall in average AST rents in 2013 – the only region to record a fall during the 2013 survey year.

Evidence also suggests that we may be beginning to see two tiers in residential rents as demand for large properties weakens with high running costs being a factor.

Proactive tenant management, along with a realistic pricing policy, will be necessary to ensure that voids are minimised and income maximised.

At the lower end it is envisaged that demand will remain strong as raising equity to buy remains difficult for many, although this may be tempered by 'Help to Buy' schemes.

A significant threat to this sector is the impending changes to the EPC regulations, which will compel landowners to make significant capital improvements to their properties before they can be let.

Commercial

Average income from all commercial sources on 'All Estates' rebounded in 2013 back to a similar figure recorded in 2010. In 2013 income from this sector represented 10% of gross income up from the 7% recorded in 2012.

This trend was similar in England. Evidence suggests that there has been more activity for commercial workspace on rural estates and it is anticipated that this trend will continue.

Similarly average income from commercial sources on 'All Estates' almost doubled in 2013 to £12 per acre (£30 per ha) back to levels recorded in 2010.

In 2013, average rental income from telecom masts fell by -15% to average £7,212 per mast. In England a similar trend was recorded although rental levels fell faster.

As well as reduced unit income, our research data suggests that the density of masts has fallen adding an additional pressure to the generation of income from this asset.

Leisure

Income from leisure activities amounted to £6.10 per acre (£15 per ha) in 2013, up 7.3% from 2012. However, it remains under pressure in contrast to the commercial sector and average leisure income represented 4.8% of gross income last year, considerably lower than the 8.7% recorded in 2010.

Again location is key and using English regional data to illustrate, the South West and South East of England recorded the highest levels of income from this sector at £7 per acre (£17 per ha) and £12 per acre (£30 per ha) respectively.

The prolonged weak economic climate has clearly had an effect on this sector. This is very evident in the key tourism area of the South West of England, where income from this sector is just a third of the £24 per acre (£57 per ha) that was recorded in 2009.

> "Evidence suggests there has been more activity for commercial workspace on rural estates and it is anticipated that this trend will continue" Savills Research

Woodland

In Scotland the average estate generated just under £5 per acre (£12 per ha) from woodland – no real change from 2012. This is in contrast to England where woodland makes no real contribution, in its own right, to gross income.

However, woodland is an important part of the estate structure/assets providing the opportunity for sporting and leisure activities.

Woodland/forestry is a resource which is worth more exploration as it represents around 14% of the area of the average Scottish estate. Potential opportunities might include renewable energy, woodland grants and leisure projects.

Sporting

Our survey shows that the average income, on lowland Scottish estates, from sporting sources is £3 per acre (£7 per ha) – similar to that recorded in 2012. However, our research shows that the range is diverse with some estates generating up to £11 per acre from sporting enterprises.

Renewable Energy

Renewable energy potentially offers estates an additional income stream, and this is the key driver on 80% of UK estates considering a project.

However, our survey results suggest that only 20% of estates have completed an audit to establish actual energy use, although 70% have assessed the renewable energy potential of their estate with another 12% planning to do so in 2013.

The main challenge in proceeding with a project (mentioned by 72% of respondents) is the capital cost/ availability of funds, with planning (22%) also being a significant hurdle.

Estate Benchmarking
COSTS

Average total expenditure across Scottish rural estates increased during 2013 by 12.3% to £96 per acre (£146 per ha). Although the largest increase for four years it was well below the increase in gross income and not altogether surprising given the inflationary pressure on costs.

Our survey shows that the two main costs, property repairs and management, represent over three quarters of all costs and almost 40% of gross income.

However, 'other costs', which increased by 13% to £13.21 per acre, represent just over 105 of gross income and should not be ignored. Anecdotal evidence suggests that the insurance market is competitive, with premium reductions achieved in some cases.

In addition, new legislation can bring added costs. In October 2012, the Government introduced a requirement for all employers to automatically enroll their workers in an approved pension scheme, to be phased in over four years for smaller employers.

Despite this new legislation, only 20% of a subset of our survey participants currently has an employee pension scheme. Whilst employees can opt out, the minimum contributions to be made by employers is 3% and this should be factored in to estate budgeting.

Average property repairs increased by 21% across 'All Estates' to £27.24 per acre, giving an annualised increase of 12.4% over the past three years. Property repairs represent just over one-fifth of gross income and towards half of total expenditure.

Capital improvements on the average estate also increased significantly – more than doubling to almost £13 per acre. The amount an estate spends on improvements generally varies greatly from year to year, particularly where estates do not have a rolling repairs programme. It is a good policy to actively manage and timetable repairs to fit in with cashflow and labour troughs.

Whilst estate repair expenditure remains consistent at 20 – 25% of gross income, capital expenditure frequently peaks following rent reviews. Particularly in the light of the Telfer case, landlords will seek to ensure that tenants are meeting their repairing obligations to mitigate against such spikes in expenditure.

Average total management costs across 'All Estates' increased by just over 1% in 2013 to just over £18.60 per acre.

TABLE 1

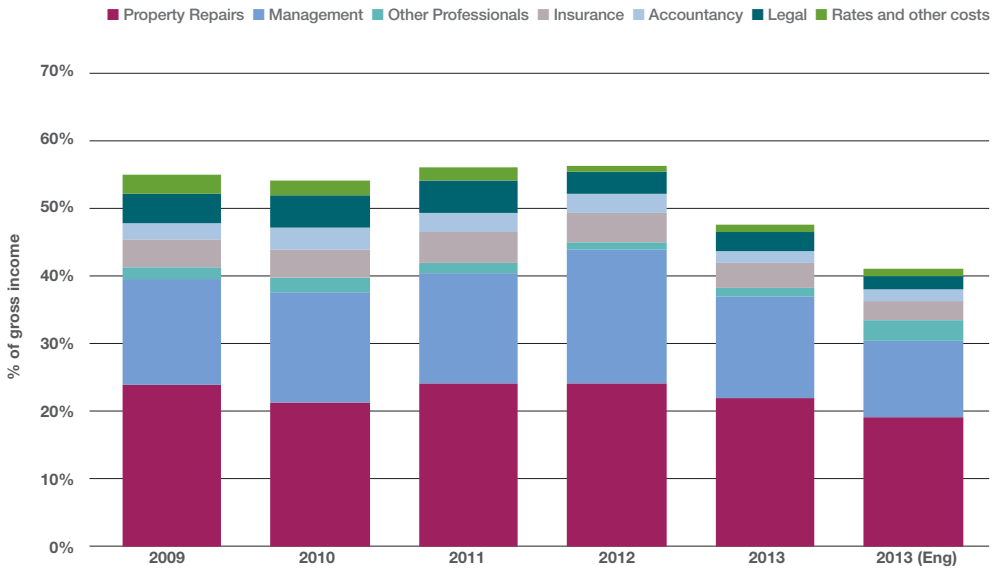
Other costs on 'All Estates'

	Average £ per acre (£ per ha)	2013 growth %	% of gross income (2013)
Insurance	£4.37 (£10.80)	3.7%	3.6%
Other professional fees	£1.71 (£14.23)	67%	1.4%
Legal costs	£3.65 (£9.02)	23.8%	3.0%
Accountancy	£2.14 (£5.29)	-19.6%	1.7%
Rates and other costs	£1.34 (3.31)	61%	1.1%

Source: Savills Research

GRAPH 6

Cost as a % of Gross Income



Source: Savills Research

Estate Benchmarking
ASSETS PERFORMANCE

Rural assets continue to outperform alternative assets and our survey again records a healthy investment performance on 'All Estates'.

In the year to 5th April 2013 the average Total Return for 'All Estates' in Scotland for all Let Property was 10.8%, the sum of a net income return of 1.3% and capital growth of 9.5%.

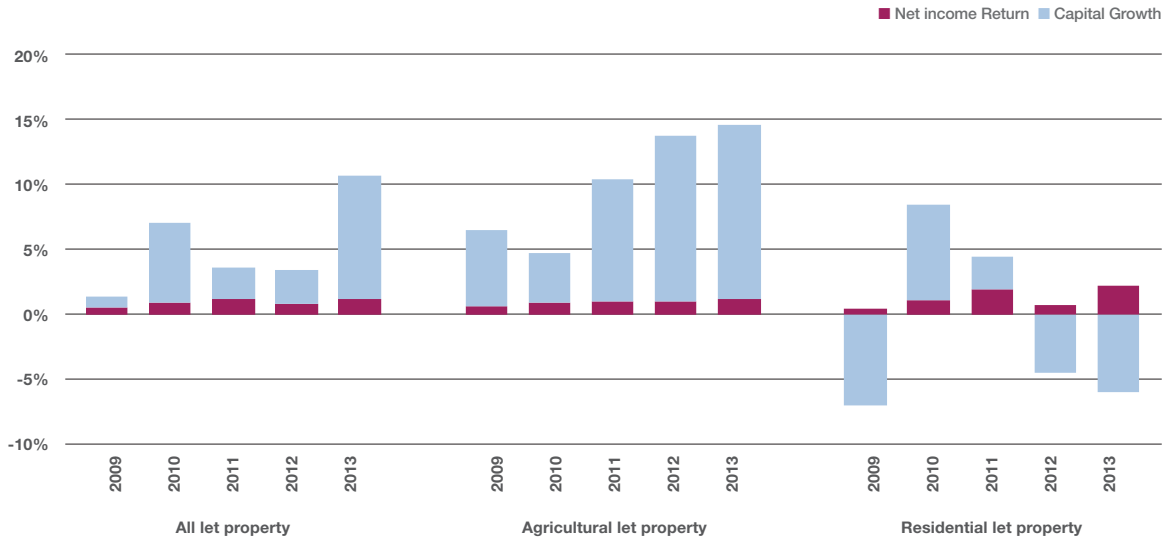
However, it is the farmland that contributes the lion's share of this performance. It recorded capital growth of 13.4% and a net income return of 1.2% giving a total return of 14.6%.

The let residential sector is currently the weakest performer on rural estates showing a similar trend to the mainstream Scottish residential markets, where values fell -4.9% in the 12 months to April 2013.

Average total return for let residential property on 'All Estates' was -3.8% being the sum of a net income return of 2.2% and capital growth of -6%.

GRAPH 7

Investment Performance



Source: Savills Research

OUTLOOK

Identifying the opportunities and threats for rural estates in Scotland

Our Estate Benchmarking Survey again reinforces the benefits of having diverse assets and enterprises to provide a steady income stream, which has kept pace with inflation. Proactive management with a continued focus on costs will be key to maintaining this position and driving more value to the bottom line.

■ There appear to be some rays of light in terms of the general economic conditions with recent indicators showing a more positive trend. The Scottish economy grew by 0.7% in the third quarter of 2013, up from 0.3% in the first quarter. However, there is no room for complacency, as output still remains 3.3% below its prerecession peak.

■ The 2013 survey results recorded the strongest income (gross and net) growth for several years. We expect average gross incomes on rural estates to continue in a steady upward direction although costs and therefore net incomes will face some pressures.

The key growth factors in the short-term are likely to be:

■ Continued growth in the proportion of houses let at SAT rents (2% per annum over the past five years) as concessionary agreements expire and agricultural tenancy reversions release houses tied up in tenancies.

■ We expect the performance of the leisure sector to improve. Visit Scotland shows a rising spend by visitors to Scotland and spend by day visitors to Scottish tourist locations increased by around 10% last year. There is scope for rural enterprises to benefit from this improving trend.

■ Growth in the proportion of LDT/SLDT area (5% per annum over the past five years) with reversion from traditional tenancies.

■ We expect agricultural rents to continue to increase, reflecting pent up demand and the outcome of recent Land Court decisions.

■ Similarly we expect the fortunes of the commercial sector to improve in line with the recovering wider economy as business confidence returns.

These positive aspects will be balanced by:

■ The uncertainty created by land reform, proposed legislative change and the Independence referendum cannot be underestimated. Such uncertainty can only serve to dissuade or delay landowners from commencing significant investment projects which would have a clear detrimental impact on the wider rural economy.

■ Pressure on subsidy income for tenants and in hand operations and managing the strategic implications on estates as the latest CAP reforms are implemented.

■ The cost of new legislation to enroll all employees in an approved pension scheme as noted on page 8.

■ Farmland (in hand and let) and forestry have an excellent track record in investment performance over the long-term and have outperformed other assets in recent years, which we expect to continue.

■ Impact of EPC legislation on rents and on expenditure on capital improvements to meet new requirements.

Savills Team

Please contact us for further information

Jonathan Henson
Estate Management
+44 (0)1738 477511
jhenson@savills.com

Kenneth Munn
Estate Management
+44 (0)141 222 5870
kmunn@savills.com

Ian Bailey
Head of Rural Research
+44 (0)1797 230 156
ibailey@savills.com

Ewan Berkeley
Estate Management
+44 (0)1356 628605
eberkeley@savills.com

Charles Dudgeon
Estate and Farm Sales
+44 (0)131 247 3702
cdudgeon@savills.com

Savills plc
Savills is a leading global real estate service provider listed on the London Stock Exchange. The company, established in 1855, has a rich heritage with unrivalled growth. It is a company that leads rather than follows, and now has over 200 offices and associates throughout the Americas, Europe, Asia Pacific, Africa and the Middle East.

Savills Edinburgh
8 Wemyss Place
Edinburgh
EH3 6DH
+44 (0)131 247 3700

Savills Glasgow
163 West George Street
Glasgow
G2 2JJ
+44 (0)141 248 7342

Savills Perth
55 York Place
Perth
PH2 8EH
+44 (0)1738 477 525

Savills Brechin
12 Clerk Street
Brechin
DD9 6AE
+44 (0)1356 628 600

savills.co.uk