
Guest editorial: Embracing ESG in valuation: a paradigm shift in the International Valuation Standards

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Introduction

The past two decades has seen a strong trajectory of adoption related to green, sustainable and more resource efficient buildings and property. For many years alongside this increasing engagement in the sustainability agenda, there has been questions about what is the “value” of sustainability? How does it contribute? What is the premium? And why are valuers not considering it? The difficulties and the challenges have been expanded on in the academic literature; some industry bodies have embraced and tried to provide guidelines and directions to valuers, like the Royal Institution of Chartered Surveyors (RICS), The European Group of Valuer Associations (TEGOVA), and the Appraisal Institute (AI) in the USA. Albeit, with limited success as reported in many academic studies. However, what was lacking was an understanding of how the market participants were engaging with the sustainability agenda, valuers’ understanding, knowledge and tools to consider the relationship between sustainability and value drivers and a requirement for inclusion in valuation.

In the last few years we have seen a paradigm shift in the industry, with both occupiers and landlords being affected by voluntary market drivers, regulation and legislation, opportunities for green (or sustainable) financing and the need to respond to changing requirements of both occupier and investor demands for more sustainable, often associated with the framework of environmental, social and governance (ESG) and net zero carbon aligned opportunities.

The evolution and changes in the market in regard to sustainability and the framework of ESG have been acknowledged by the International Valuation Standards Council (IVSC) in their International Valuation Standards (IVS), by including directions to valuers regarding ESG.

The IVS are recognised as a key framework for valuing assets and liabilities in markets worldwide. These standards govern many countries’ valuation practice, and have ensured consistency, comparability and transparency to the valuation process in over 100 countries. In response to ESG becoming mainstream in the global markets, it has become imperative to integrate ESG criteria into valuations. The updated IVS, set to take effect from January 2025, now include specific guidance for valuers to consider ESG factors in their assessments.

The IVS now recognises ESG as a critical aspect of valuation practices by directing valuers to consider the impact of sustainability, ethical practices, financial performance and operations of assets or liabilities. The inclusion of ESG within the Valuation Approaches section of the IVS, directs valuers in their process of assessing comparable transactions, to consider ESG factors alongside traditional valuation considerations like size, quality and other material characteristics. This integration acknowledges the growing importance of sustainability and ethical practices in today’s business landscape.

The inclusion of ESG in valuations presents both challenges and opportunities for valuers globally. Whilst the IVS provide a list of ESG categories, to successfully incorporate ESG criteria into their assessments, valuers will need to identify reliable ESG metrics and reporting frameworks that can be consistently applied. Further, valuers will need to enhance their knowledge surrounding ESG, including up-skilling and familiarisation with ESG-relevant criteria specific to their regions and local markets. A particularly aspect that will need localised examination is how the IVS defined ESG parameters may map against existing sustainability and green rating certifications utilised within local markets. Additionally, the evolving legislative and regulatory environment is escalating at multiple levels of government.



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For example, like the EU taxonomy requirements in Europe, to the Minimum Energy Efficiency Standards (MEES) in the UK, and more broadly the role the International Sustainability Standards Board (ISSB) reporting requirements and how this is being adopted by countries, requiring companies and organisation to report on Scope 1, 2 and 3 emissions and climate-related risks.

The voluntary and mandatory expectations of ESG further complicates markets and the actions of the various market stakeholders. Further, since Covid-19 there has also been enhanced focus on the “S” in ESG. Consequently, the growing importance of ESG considerations in investment and business decisions, along with mandatory reporting requirements, creates a valuable opportunity for valuers to play a crucial role in providing meaningful insights and recommendations to their clients.

It is important to consider the local and global ESG landscape, information availability and benchmarking options when applying ESG considerations to real estate valuations. The educational component is equally vital, as valuers must understand the implications of ESG data and its meaning within the valuation context.

The inclusion of ESG criteria within the IVS represents a significant milestone for the valuation profession. As sustainability and ethical practices gain prominence across global markets, valuers must adapt their practices to consider the various dimensions of ESG in their assessments and valuations. The transparency and level of scrutiny arising from mandatory reporting of emissions and climate-related risks will influence market stakeholder decision making and consequently affection both transactions and valuations. While challenges lie ahead, valuers who develop their knowledge and awareness, and incorporate ESG considerations effectively will be well-positioned to provide valuable insights to clients and contribute to a more sustainable and responsible built environment.

This Special Issue delves into the questions around the value of ESG, implications of green and “S” for finance considerations, options for sustainability scoring to assist in pricing processes and understanding how the IVS definition of ESG and associated categories map against longstanding existing market adopted sustainability certification tools.

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