

# BCSC Conference & Exhibition

Bridgewater Hall and Manchester Central

Mon 9 - Wed 11 Nov 2009

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SHAPING RETAIL PROPERTY

# Educational Workshops

## Sustainability

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PRUPIM

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# Sustainability, responsible property investment and shopping centres

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*Chair – IIGCC Property Workstream*

**Presentation to BCSC conference**

**London, 10<sup>th</sup> November 2009**

Part of the M&G Group

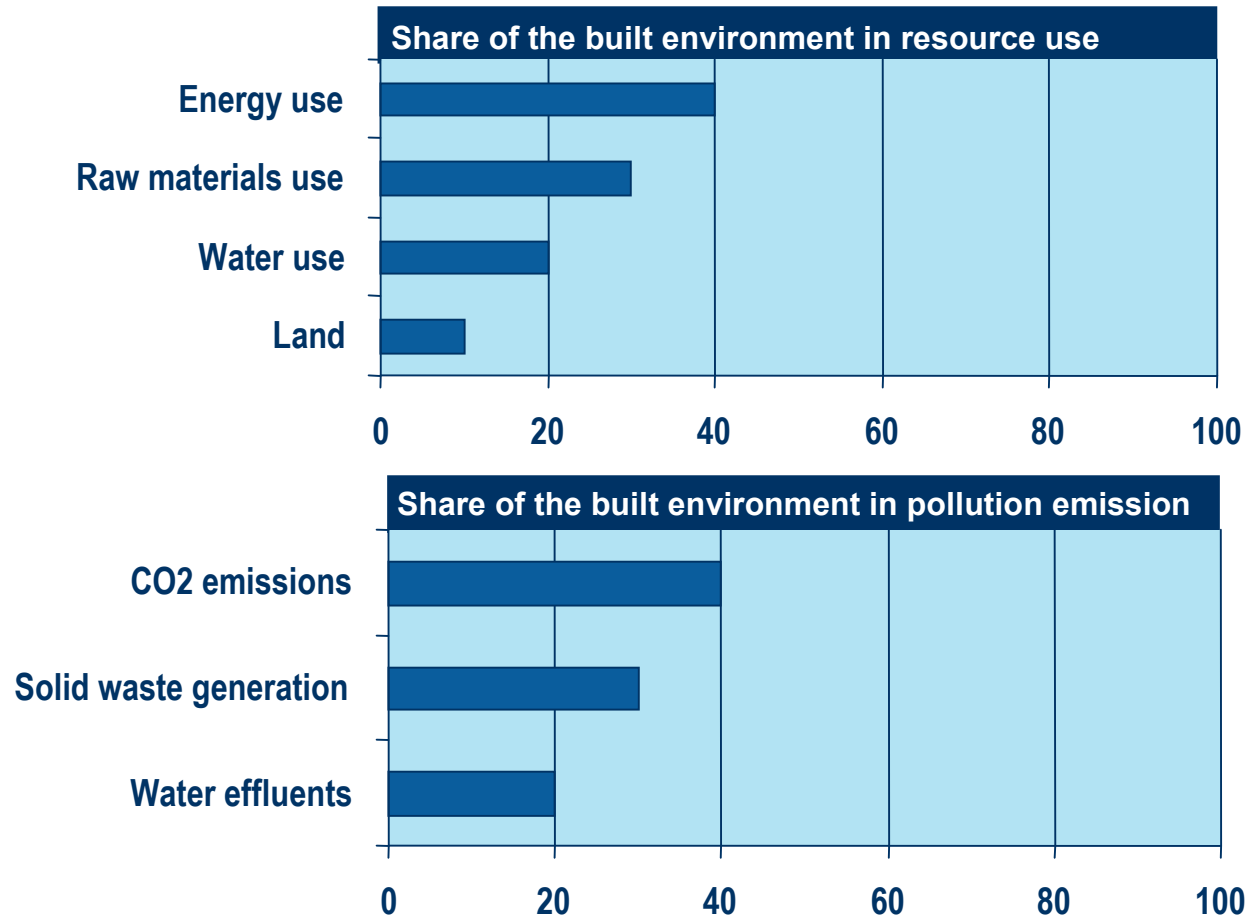
**PRUPIM**

- Property (including retail) – an important part of the problem and the solution
- Can responsible property outperform?
- What might responsible property investment look like in the shopping centre sector?

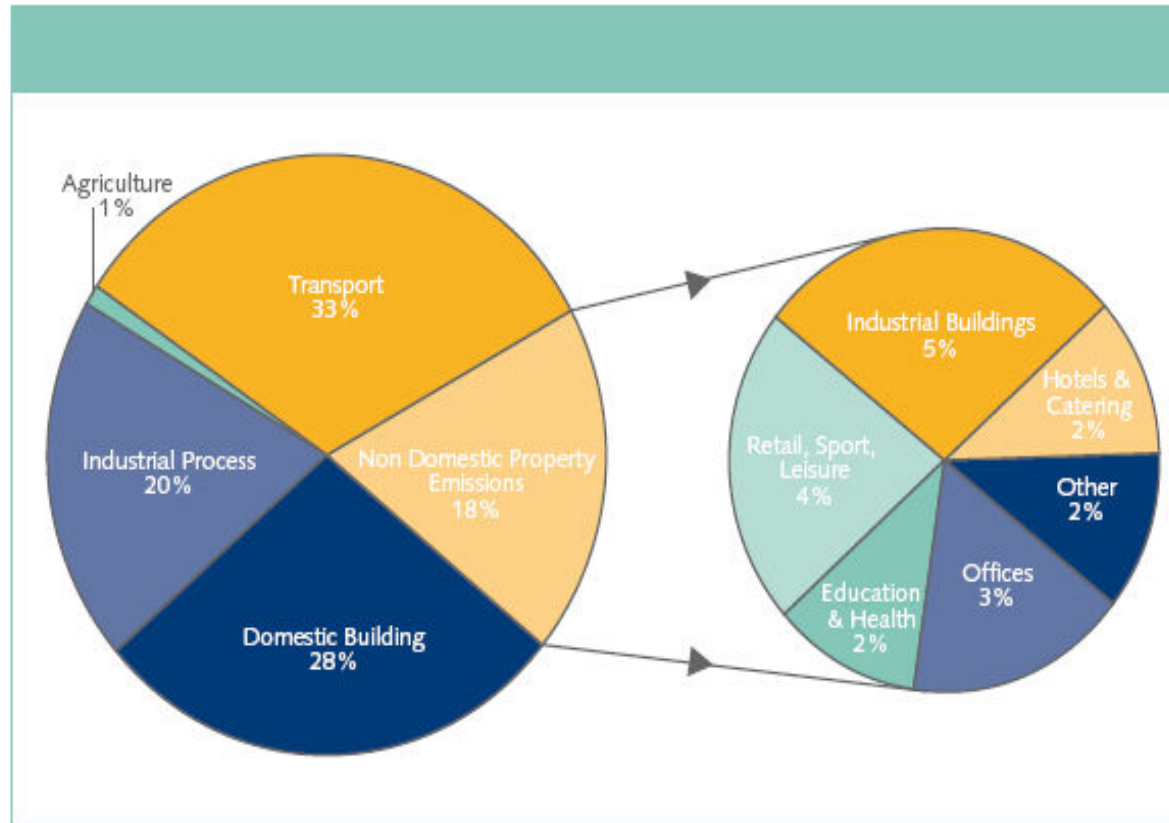
# Property and Climate Change

Being a significant part of the problem....

REAL ESTATE  
INVESTMENT  
MANAGEMENT



# And, ....shopping centres?



- If 'retail, sport and leisure' = 4%\*; Shopping centres = (guess 2%)
- But every per cent counts and this is a lot of CO2 emissions to go for

# Property – a key part of the solution

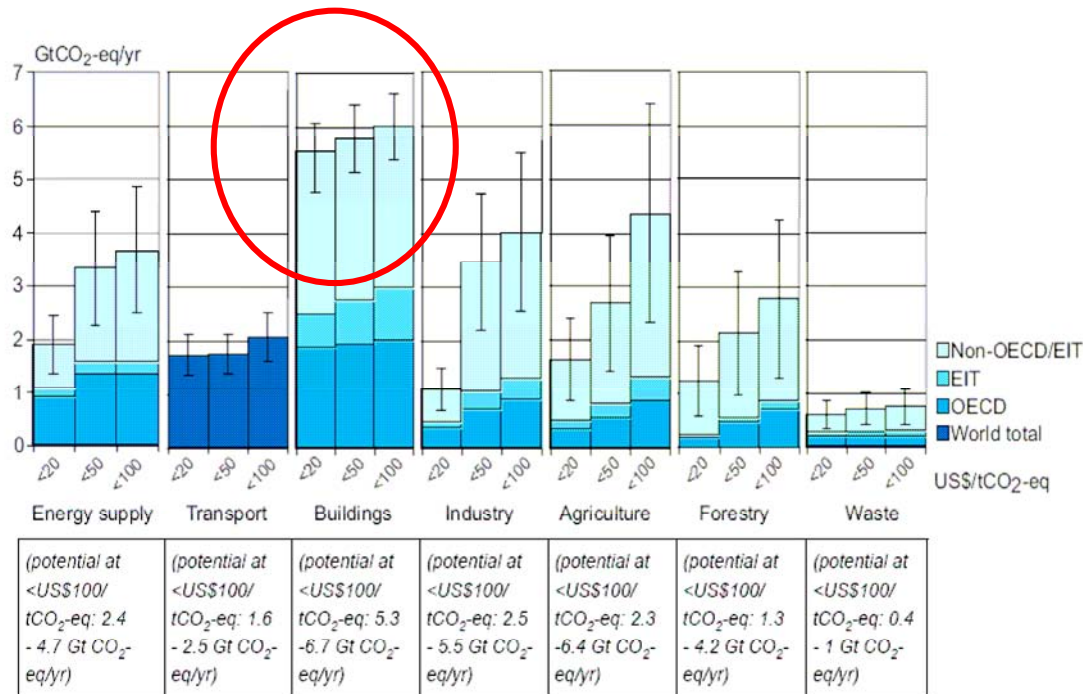


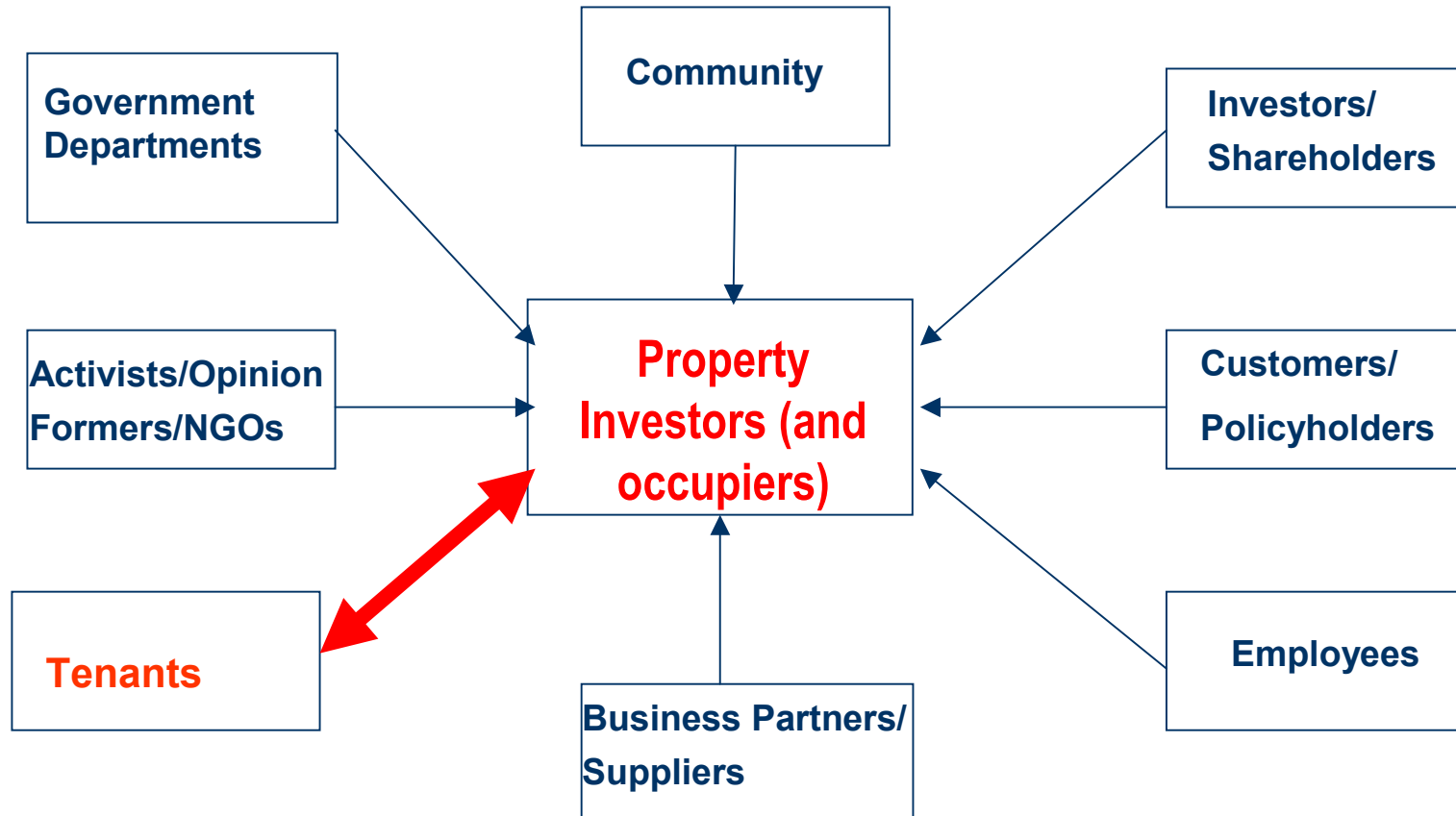
Figure SPM.6: Estimated sectoral economic potential for global mitigation for different regions as a function of carbon price in 2030 from bottom-up studies, compared to the respective baselines assumed in the sector assessments. A full explanation of the derivation of this figure is found in Section 11.3.

*“(S)ubstantial reductions in CO<sub>2</sub> emissions from energy use in buildings can be achieved over the coming years using existing, mature technologies for energy efficiency that exist already and have been successfully used.*

*“There is also a broad array of widely accessible and cost-effective technologies and know-how that can abate GHG emissions in buildings to a significant extent that has not as yet been widely adopted.”*

# Property/Shopping Centres in the Spotlight....

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Fund managers are asking - *can  
responsible real  
estate outperform?*

# Consider three possibilities....

**Behaving Responsibly  
Enhances Fund  
Performance**

**Fiduciary Duty  
to act this way**

Can we find a logic  
for this?

**Behaving Responsibly  
Has No Effect on Fund  
Performance**

**“Moral” Duty to  
act this way**

Can we invert this  
logic and do things  
that do not affect  
fund performance?

**Behaving Responsibly  
Harms Fund Performance**

**Dilemma**

Many start here...

# A logic for enhancing performance through behaving responsibly ?

REAL ESTATE  
INVESTMENT  
MANAGEMENT

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Dilemma

# RPI can have a positive effect on property values and returns

## *Setting aside the risk of unanticipated Government regulation.....*

Factor	Investment Implications	Underlying effects
Tenants prefer green buildings	<ul style="list-style-type: none"><li>▪ Rental differentials emerge between green and non-green buildings</li><li>▪ Green assets quicker to re-let</li></ul>	<ul style="list-style-type: none"><li>▪ Rental growth higher, depreciation lower</li><li>▪ Shorter interruptions to cash-flow, lower risk premium</li></ul>
Green buildings are cheaper to run	More money available for rent	Rental growth higher
Other investors prefer 'green' buildings	Green properties quicker to transact	Greater liquidity, lower opportunity cost and risk premium

- Green assets likely to have lower yields, higher values over time
- As differences in value emerge, green assets should outperform
- The more it matters – the more it will impact value and performance

# Early evidence from the office sector...?

## Results for buildings with Energy Star ratings

Variable	Impact of being 'green'
Rent per square foot	+3%
Effective rental income (adjusted for prevailing occupancy levels)	+6%
Sale prices	+16%

- Total sample of 9,998 office buildings throughout the USA – 893 “green”
- 1,816 offices sold between 2004 and 2007 – 199 “green”
- Rental information on 8,182 – 694 “green”

Source: Eichholz P, Kok N and Quigley J (2009) Doing Well by Doing Good? Analysis of the Financial Performance of Green

We need evidence from the shopping centre market

# Does acting on this knowledge make for a responsible investor?

- Sustainability is changing the context in which property investment decisions are made
- **Successful investors** will understand and exploit this

**BUT**

- **Responsible investors** will go further and look for economic ways to work with assets and tenants to improve the environmental and social credentials of assets and, thereby, protect or enhance future returns



Low cost, no cost and  
economic action



# Economic action

REAL ESTATE  
INVESTMENT  
MANAGEMENT

Behaving Responsibly  
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**Dilemma**

# PRUPIM's (internal) Improver Portfolio

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MANAGEMENT

- What can we achieve without jeopardising our fiduciary responsibilities - through low, no or other economic asset management?
- Mixed portfolio of c£500 million of typical assets (including a shopping centre) taken and economic measures used to lower their environmental footprint
- Double 'benchmark'
  - Provide competitive returns with the relevant IPD benchmarks
  - Exhibit diminishing environmental impacts against a Day 1 benchmark
- Use learning to inform property and asset management across the other £15billion of property we manage

# Setting priorities: (Shopping Centre example)

	Low Cost	Medium Cost	High Cost
High Impact	<ul style="list-style-type: none"> <li>Waste management for landlord</li> <li>Apply an Energy Management System</li> <li>Water conservation for landlord</li> <li>OPR for landlord</li> <li>Energy management M&amp;T for landlord</li> <li>Apply ISO 14001</li> </ul>	<ul style="list-style-type: none"> <li>Waste Management scheme for tenant</li> <li>OPR tenants area</li> <li>Water conservation for the tenant</li> </ul>	<ul style="list-style-type: none"> <li>Energy management M&amp;T for tenant</li> <li>Fully inclusive leases</li> <li>Renewable on-site energy generation</li> </ul>
Medium Impact		<ul style="list-style-type: none"> <li>Renewable energy bought in for landlord</li> <li>Tenant selection and use</li> <li>Tenant security and safety</li> <li>Alienation provisions reviewed – bar on assignment to unwanted tenant types</li> <li>Green travel plan</li> <li>Standard traditional lease</li> </ul>	<ul style="list-style-type: none"> <li>Renewable energy bought in for tenant</li> <li>Tenant education</li> <li>Catering</li> <li>Suppliers</li> </ul>
Low Impact	<ul style="list-style-type: none"> <li>Landscaping materials</li> <li>Cleaning materials</li> <li>Hardstanding</li> </ul>	<ul style="list-style-type: none"> <li>Cycling facilities</li> <li>Engage with local community</li> </ul>	<ul style="list-style-type: none"> <li>Tenant morale and welfare</li> <li>Business travel data</li> </ul>

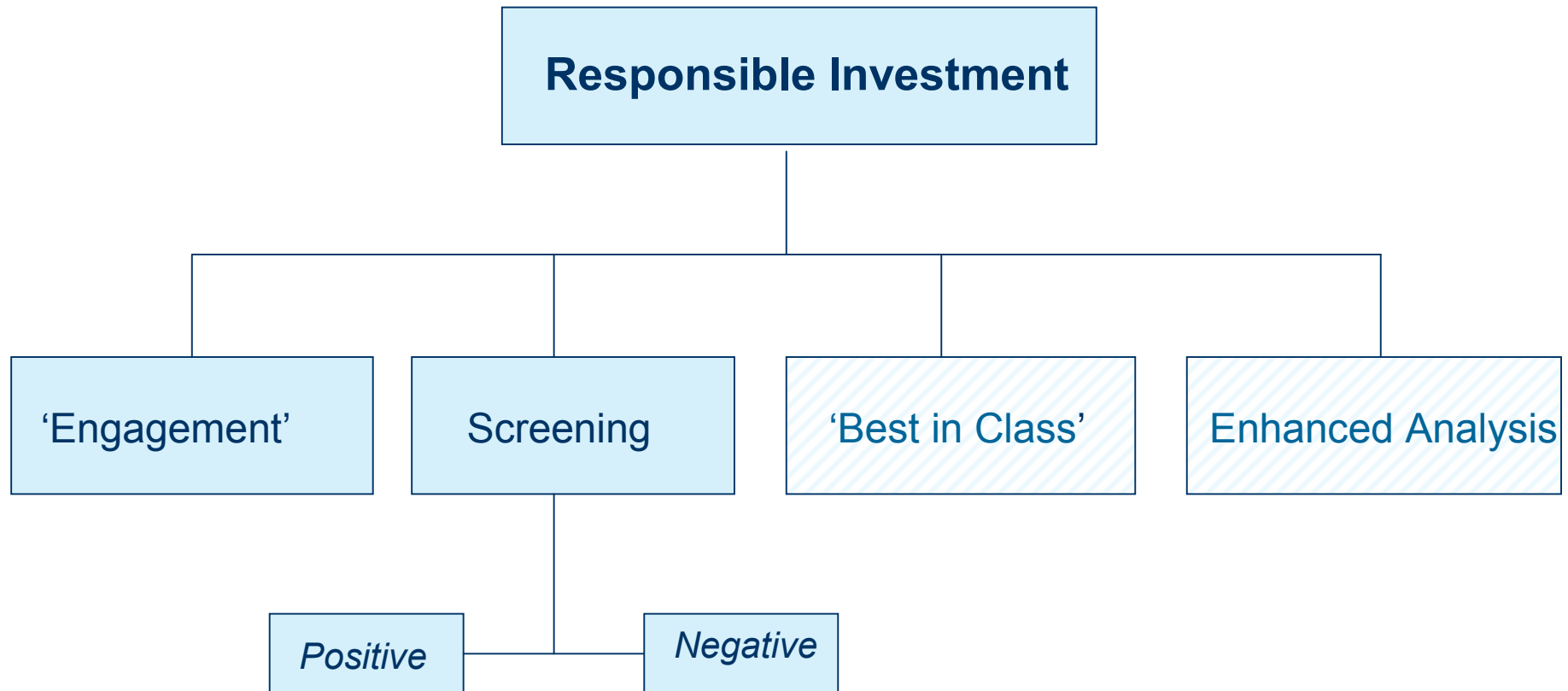
**Low and no cost - high impact actions**

# What might responsible property investment look like?

*“(SRI is) where social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments, and the responsible use of rights.....attaching to investment”* (Mansley M., 2000, pg 3)

# Socially Responsible Investment - main approaches in equities

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**Direct Action**

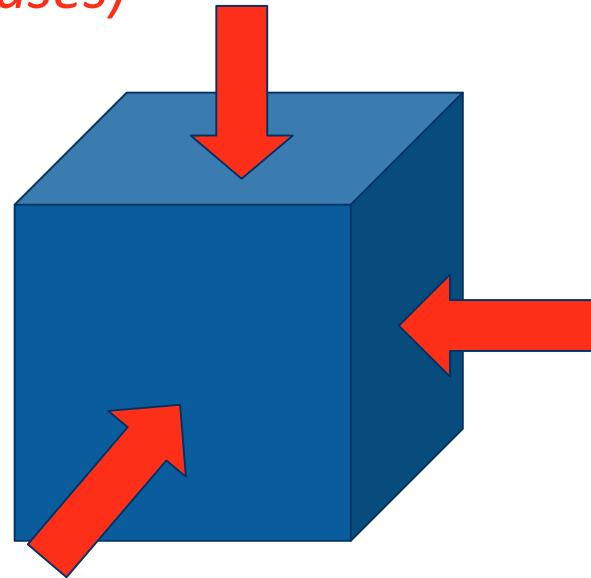


**Indirect Pressure**

# Three forms of 'Engagement' in Property

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*Engagement with the 'Legal Structure'  
(leases)*



*Engagement with the  
Occupier (and, of  
course, tenant with  
landlord)*

*Engagement with the Built  
Structure (buildings)*

- On Site
  - New building – rare but offers complete control
  - Refurbishment – potential for meaningful improvements
  - Property management - small but myriad beneficial actions
- “Situation”
  - Travel plans, etc..
- Stop – start
  - Shopping centres - always occupied but greater scale and more common parts

# Engagement - with occupiers

- Occupiers are crucial to the environmental and social impact of a property
- Split interest issue
  - where the economic benefits of progressive actions do not accrue to those trying to conserve
- ‘Informal engagement’ between landlord and tenants
  - No ‘voting’ rights, as in equities
  - Dialogue to persuade or educate how to utilise their premises in a more environmentally responsible way.
- Clearly – occupiers can be demanding of their landlords

- Green leases/Memoranda of Understanding
  - obligations on both tenant and landlord, agreed at the outset and enforced through the term of the lease, to
    - work collaboratively to improve the environmental performance of the building
    - Share relevant information about electricity, gas and water consumption, waste management, and plant maintenance
    - Set up Building Management Committees to review environmental performance, agree environmental management plans and produce progress reports
    - Etc...

# Screening Property assets – problematic?

- Limited number of relatively uniform and legacy assets
  - Ease of screening within the sector? ‘Much of a muchness’?
  - Across property asset types – do shopping centres fare well? ( location of properties, physical attributes of buildings, and/or tenants )
  - Limited liquidity
- Tenant screening? – very problematic
  - ‘One bad apple?’ and who says so anyway?
  - Assignment rights
  - Capital already invested – make being ‘choosy’ hard
  - Limited data – on which to judge tenants or buildings

# Conclusions

- Property is a major element of both the problem of, and the solution to, increasing CO2 emissions
  - A very major user of resources generally and conduit for CO2 emissions
  - The lowest cost per unit impact on the problem
  - Shopping centres are a high profile and obvious focus for action
- Even setting aside increasingly stringent government regulations – ‘green’ property investments should perform better
  - Higher net income growth at lower risk
  - Savvy investors will profit on this; responsible investors will strive to ***‘do well by doing good’***
- Shopping centres offer exceptional engagement opportunities to lead the fight against CO2 emissions growth



# Appendix



# But... (shopping centre) property is different to equities

- Relationship between Investor and Invested Asset
- Property - the '3-D' Asset
- Property - a Concatenation of Time-limited Investment Events
- Differential Liquidity and Transaction Costs
- Property - 'Legacy Stock'

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