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Is sustainability really influencing investment decisions?

Sustainability is redefining the balance in real estate investment decision-making. Whether the objective is creating value, reducing cost, or protecting assets against early obsolescence, the combined drivers of regulation and growing stakeholder interest in most markets means that sustainability is increasingly seen as an important commercial consideration in property decisions. The continuing challenging economic conditions appear to have helped sharpen the focus around sustainability, despite misgivings amongst sceptics.

Cushman & Wakefield conducted research that involved in-depth interviews with managing directors and senior fund managers from 28 European real estate investors. The results painted a picture of a fast changing landscape where sustainability was becoming an increasingly important consideration in investment decisions, despite the lack of quantifiable evidence of the financial costs or benefits associated with this issue.

In 2012, 96% of respondents had implemented a sustainability policy at the fund level, compared to 40% in 2011. Almost 90% of investors and fund managers we spoke to now have processes in place to evaluate potential new acquisitions in terms of sustainability. Of these, 84% now use a consistent methodology to evaluate the sustainability credentials prior to acquisition of properties. There is a commonly held belief amongst investors that sustainability is already impacting value, and that poor sustainability credentials pose a significant risk to the value of a property.

The majority of interviewees are seeing occupiers demanding more sustainable space. There appears to be an increasing consensus that sustainability delivers added value through properties that are quicker to let, especially in difficult markets, that are cheaper to run and that attract better quality tenants with stronger covenants.

Respondents were asked to list (in order of importance) those sustainability factors that they felt would have the greatest impact on the value of a specific property. Unsurprisingly, energy performance and utility consumption are seen as the primary drivers for impacting value, although other factors that can be directly linked with operating costs (e.g. waste management, water) are becoming more important.

“What we are seeing is a strong step in the right direction. The real challenge for all however is converting policies into real savings as this is what occupiers are demanding. This is where the real challenge begins as instant solutions are difficult and many buildings require investment to achieve sustainability targets,” says Colin Glover, Head of Project Management at Cushman & Wakefield Slovak and Czech Republic. Achieving this balance requires the involvement of all property participants from the owners to the occupiers to the facility management team all working together to achieve benefits for all.

Although there is a widespread acceptance that a value differential exists, the evidence remains largely anecdotal. A few investors and fund managers report instances where a rental premium was being achieved for sustainable buildings. These premiums are generally most apparent in office space in specific markets such as Australia, USA, the Netherlands and Germany. The lack of clarity inevitably means it remains difficult to accurately reflect sustainability in financial decision making. Given the diverse opinions regarding value differential, unsurprisingly less than a quarter of respondents said that they are currently applying adjustment factors to yields to take account of sustainability.

From my point of view, the sustainability trend is not so profound in Slovakia yet. In Slovakia, developers are now starting to embrace the various certifications such as LEED and BREEAM although the process lags behind the progress made in Western European countries. Whilst our survey demonstrates that there is a global firming of opinions in this regard, I don’t yet see sustainability as the driver yet for occupier’s decisions. In my opinion, one of the first steps is to encourage existing landlords to have in place an Energy Performance Certificate. This provides a statement of the energy efficiency of the building and operations and the certificate is actually part of EU Law. Despite this, I would estimate that a maximum of 20% of commercial buildings actually have this in place in Bratislava. It’s a surprise to me as this relatively inexpensive document can demonstrate the quality of both the building and property management and is a differentiation tool. As a perfect example, Apollo Business Centre which despite being completed in November 2004 was successful in securing a rating of ”B” for energy performance (the second best possible out of seven ratings). This also helps to demonstrate to occupiers that buildings, whilst not “brand new” are still competitive.

When combined with increased pressure from funders, reports of escalating occupier demand in the prime office market, increasing regulatory requirements, and the expectation that energy costs will continue to rise in the future, it is clear that a critical mass has been reached in some markets and that the industry now finds itself at an interesting tipping point.

There is no doubt that tomorrow will be a more energy-efficient world. What appears to be less widely known is that there are steps now that landlords and developers can and should be doing to get ready for tomorrow.

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