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# UK real estate embraces carbon neutrality

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Real estate | September 2021

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*Huge cuts in emissions from real estate assets will be essential to reach net zero carbon by 2050. Columbia Threadneedle Investments' carbon neutral real estate approach has been established for over a decade and offers major benefits for all stakeholders.*

A carbon-neutral approach to real estate is a strategy whose time has come. Over the past 18 months a series of factors have combined to make this a natural choice for real estate tenants, landlords and investors. As the effects of climate change intensify, pressure is growing to step up the world's response and reach the target set by the 2015 Paris Agreement to limit global warming – net zero carbon by 2050.

Within the UK, non-domestic buildings account for around 18%<sup>1</sup> of the country's total emissions, which means real estate owners and investors have a huge part to play in achieving that goal. According to the Carbon Trust, a leading UK-based environmental and sustainability consultancy, carbon emissions from UK commercial property must decline by at least 80% if the country is to reach net zero emissions.

## Improving ESG performance

At the same time, companies that occupy these buildings are under pressure from investors and civil society to improve their ESG performance. And, of course, the pandemic has changed the way people work, shop and spend their leisure time, forcing companies to rethink their real estate needs and adapt their spaces to make them safer and more attractive for employees and customers.

The conclusion is clear. Real estate markets are undergoing a period of rapid change and their direction of travel will inevitably be towards net zero carbon emissions. Against this background and as an industry pioneer, Columbia Threadneedle has been partnering with the Carbon Trust and key developer Stanhope since 2010, to create a comprehensive framework for delivering carbon neutral assets in one of our UK real estate strategies.

## Why the time is right

Disruption caused by the pandemic has created attractive opportunities to acquire real estate assets and refurbish them to create modern, energy-efficient workplaces in the UK, where Columbia Threadneedle manages some £8 billion of real estate assets<sup>2</sup>.

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<sup>1</sup> Source: Digest of UK Energy Statistics; BRE.

<sup>2</sup> Source: Columbia Threadneedle Investments, as at 30 June 2021.

Currently, we are seeing limited competition to acquire institutional-quality assets in the UK that require active management to unlock value, and we believe 'core-plus' and opportunistic properties are currently mis-priced. This is especially true since the UK market is at an inflection point, with economic recovery under way and gross domestic product forecast to jump 7%<sup>3</sup> this year.

These favourable market conditions provide a strong tailwind for our carbon neutral approach. Columbia Threadneedle concentrates on refurbishing buildings to bring them up to 2050 standards, both because it is quicker, cheaper and less risky than redevelopment and because retaining building structures results in significantly lower carbon emissions overall. Also, newbuild properties have embedded carbon – the carbon created in building them – whereas with existing assets, it can be assumed that the carbon is already spent.



*This London city fringe office building underwent a £14.5m carbon efficient refurbishment program by Columbia Threadneedle, acquiring an improved energy performance certification (EPC) from F to B, whilst delivering strong rental and capital growth. For illustrative purposes only.*

### Boosting energy efficiency

The key element of our refurbishment blueprint is to improve energy efficiency through measures such as LED lighting, the replacement of gas for heating purposes, improved energy controls, installation of CO<sub>2</sub> sensors to gather data on energy use, rainwater harvesting and provision of charging points for electric vehicles. Upon project completion, occupiers receive ongoing support from Carbon Trust experts to help them minimise their energy costs and carbon emissions.

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<sup>3</sup> Source: IMF, *World Economic Outlook Update*, July 2021.



*A key element of our refurbishments is to improve the energy efficiency of our properties. Typical installations include (from left) rainwater harvesting, CO2 sensors and EV charging points. For illustrative purposes only.*

We have also been working with Stanhope, a leader in sustainable development techniques, to reduce carbon emitted during the construction phase. Stanhope played a key role in the creation of the Building Research Establishment Environmental Assessment Method (BREEAM) accreditation system in the 1990s and is founding partner of the UK Green Building Council. Wherever possible, our refurbishments use recycled and sustainable materials such as carbon-negative carpet tiles and airlite paint.



*Following our refurbishments which included an upgraded façade, full M&E replacement and car parking spaces removed in favour of cycle bays, this building in Richmond London fetched an ungeared IRR of close to 52.4% over a period of 16 months<sup>4</sup>. For illustrative purposes only.*

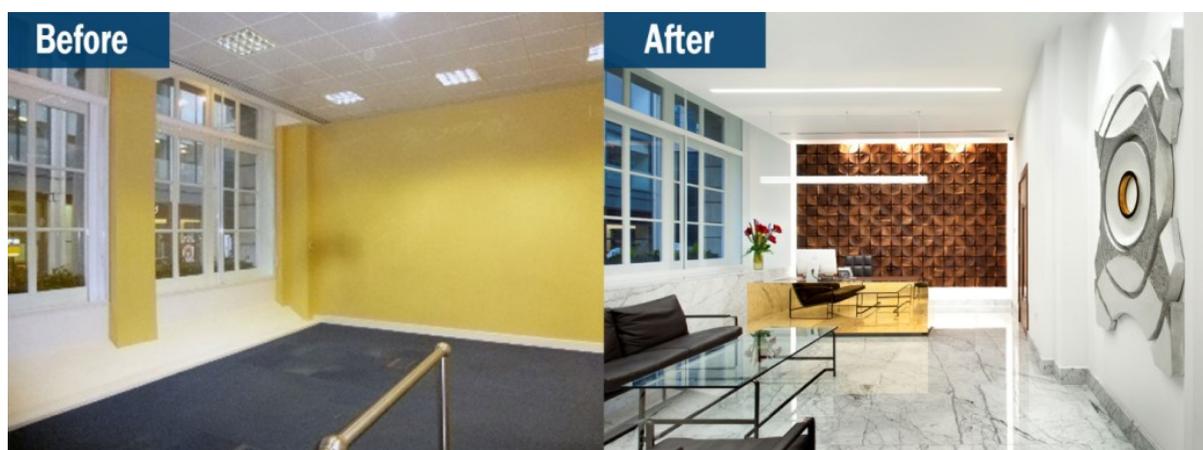
<sup>4</sup> Source: Columbia Threadneedle Investments, based on values calculated from asset purchase (Apr 2013) to post refurbishment (Aug 2014). IRR refers to internal rate of return. Past performance is not an indicator of future returns.

Finally, where remaining carbon balances must be offset to achieve net zero, we use Gold Standard or Verified Carbon Standard projects such as the Tropical Mix Reforestation project in Panama.

### Delivering value to all stakeholders

Columbia Threadneedle's carbon neutral approach to real estate is designed to deliver value to all stakeholders. As an asset manager and landlord, we can directly control only a small proportion of emissions – far more are generated, for example, by the business activities of our tenants. By making carbon neutrality the most attractive option for all stakeholders, we can create the right conditions for everyone to work together.

The risks if we do not collaborate are serious: the value of low-performing real estate assets will suffer as demand for them declines and new regulation threatens to make them obsolete. However, if we can plot an effective route to carbon neutrality we will protect and enhance their value. Our refurbishments will modernise them, delivering more attractive and sustainable workplaces with lower running costs that comply with the toughest environmental standards. This will help our tenants and investors to improve their own ESG performance, delivering wider benefits to society. For investors, our approach should translate into higher occupancy, fewer voids, higher rents and enhanced capital values.



*Our refurbishments can modernise properties and deliver more attractive and sustainable workplaces for our tenants. Above is the reception area of an East Central London office building, before and after a refurbishment project managed by Columbia Threadneedle. For illustrative purposes only.*

### Enhancing assets, returns and environments

We have already witnessed the effectiveness of our carbon neutral approach to refurbishment. For example, we undertook an extensive refurbishment of a 41,000 sq ft industrial warehouse in the UK, where we upgraded the perimeter wall insulation, fitted double-glazed rooflights and LED lighting, installed charging points for electric vehicles and provided cycle bays and shower facilities to encourage green commuting. The building's EPC rating improved from D to B and it was leased on completion for a 10-year term with a 33% rent increase. Its capital value was lifted by more than 46%<sup>5</sup> within six months from pre- to post- refurbishment.

<sup>5</sup> Source: Columbia Threadneedle Investments, based on values calculated from pre- to post-refurbishment, Q1 19 to end Q2 19. Past performance is not an indicator of future returns.



*New double-glazed rooflights, LED lightings and EV charging points are just some of the few upgrades that we installed at this warehouse, achieving a capital value uplift of more than 46%. For illustrative purposes only.*

Overall, our refurbishments to date have all achieved BREEAM “Excellent” ratings along with an average improvement in EPC ratings from E to B. Once occupied, their energy intensity is 24% lower than the typical 2019 level calculated by the UK’s Better Buildings Partnership.

This is the kind of performance that all commercial real estate assets will need to achieve if the global drive to reach net zero carbon by 2050 is to succeed. Before long, a carbon neutral approach to real estate will no longer be the exception – it will be the industry standard.

### [UK real estate at Columbia Threadneedle Investments](#)

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