

ESG Is An Opportunity For Savvy CRE Players



Environmental, social and governance (ESG) is of increasing importance as a business consideration for developers and commercial real estate (CRE) investors.

Changing World

In May 2022, Aeon Investments published a report called ESG in Commercial Real Estate Lending. In this, they write: “We are now poised at the threshold of the next phase where creating impact through sustainability and active pursuit of ESG opportunities is expected to not only generate competitive financial returns but also address societal challenges.”

For ESG advocates (and future generations), the shift in thinking couldn’t come soon enough. The Aeon report further cites research that finds “global real estate investors found that 93% of investors now include ESG criteria in investment decisions, while 83% have seen an increase in investor demand for sustainability disclosure”.

Push and Pull Factors

The change is happening on both sides of supply and demand, the report says. “ESG-compliant real estate assets,” the report authors explain, “attract lucrative, discerning tenants who are increasingly seeking efficient, healthy, and green-certified buildings”.

Even factoring in higher development and operating costs, the report includes case studies showing how developments implementing sustainable technologies attract higher rental income and result in net higher cash flows for distribution.

In the FTAdviser analysis of the report, they highlight that given all of the above, ESG will be a funding concern too, writing: “projects with poor ESG credentials will increasingly face issues accessing finance, resulting in limited options and punitive borrowing terms in the medium term”.

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Risk Management

Of course, ESG is also a key matter for CRE environmental risk management. Property owners and investors must be forward-thinking in terms of the climate-change risks a certain site, development or city will face.

As data broker Trepp's recent three-part coverage on the topic argues: "Climate change issues, recently exemplified by an abundance of fires in the West and hurricanes in the Southeast, continue to pressure insurance rates". They point to media coverage on carrier losses and rising insurance costs ("often double-digit increases") in Florida following two recent extreme weather instances.

This is why, they say, "Trepp has recently integrated data from RMS into its platforms and now reports risk scores for properties backing [Commercial mortgage-backed securities (CMBS)] loans."

Bottom Line

In the PWC and Urban Land Institute report '2021 Emerging Trends in Real Estate,' the authors highlighted how climate change and decarbonization strategies are more and more a key element of how CRE companies are doing business.

Amid all the bad news of 2022, at least we can chalk this one up for the positive column: Not only is implementing solid ESG principles now considered a business imperative, it can also be an opportunity and value-add for CRE around the world.

