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Net zero in real estate

2024

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Net zero in real estate 2024

As the new year dawns, Verco has been reflecting on the progress towards net zero carbon in the built environment. Based on responses from our net zero in real estate survey and insights from our experienced team, this report summarises sector reflections on 2023 and sustainability goals and priorities for 2024.

2023 in review

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Challenges for the climate crisis in 2023

It was never going to be easy, and 2023 was another complex year in the NZC landscape. From ice storms in Texas to wildfires in Europe, extreme weather events hit the headlines across the world, and the global stocktake[1] showed us just how far off course we are from limiting global average heating to 1.5 degrees.

Progress was made at COP28 in December, but the crucial 'phase-out' phrase didn't quite make it into the final agreement. Yet, there were encouraging developments too; we saw huge increases in renewable energy ambition and deployment and a series of guidance, frameworks and regulations were launched to support good practice and decision making in the corporate world.

Drivers for change

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The built environment is a core source of carbon emissions and a space for fresh ambitions and innovations to reduce them. At a practical level, 2023 saw several key developments including:

Additional guidance for defining transitional risk (Version 2 of the CRREM Tool), now being used as a fundamental input to the SBTi's Buildings Guidance.

A new WGBC framework for integrating social impact considerations in decision-making.

New disclosure standards covering EU, UK and US markets (CSRD, FCA SDR and the SEC CRD).

Guidance from PCAF on quantifying emissions from investments.

An update to the RICS Whole Life Carbon Assessments guidance.

Net zero carbon is an important part of ESG

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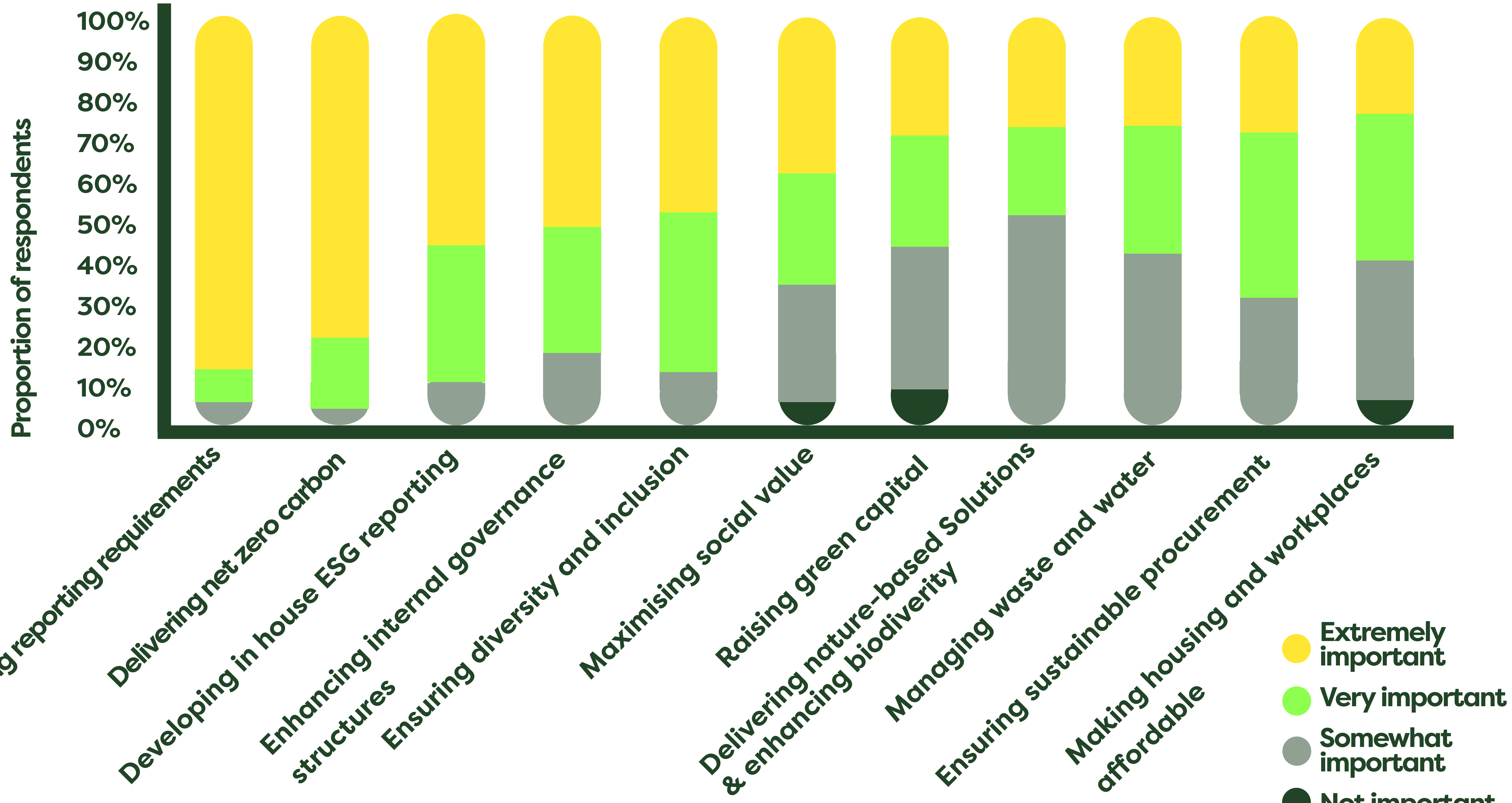
In 2015, all 193 of the UN's Member States agreed on 17 Sustainable Development Goals. Within the corporate world, these goals are often distilled into a broader acronym: ESG (Environmental, Social and Governance). While interrelated, these three areas have often been addressed independently, with greater focus placed on certain aspects over others.

Net zero carbon is an important part of the ESG puzzle, and it interlocks with other pieces; in the long term, climate change impacts societies as well as ecologies, and it's important to consider how net zero strategies can contribute to social value and enrich internal governance structures. This is reflected in our survey; 'delivering net zero carbon' has been rated as an extremely important ESG priority by our survey respondents.

ESG priorities for the built environment



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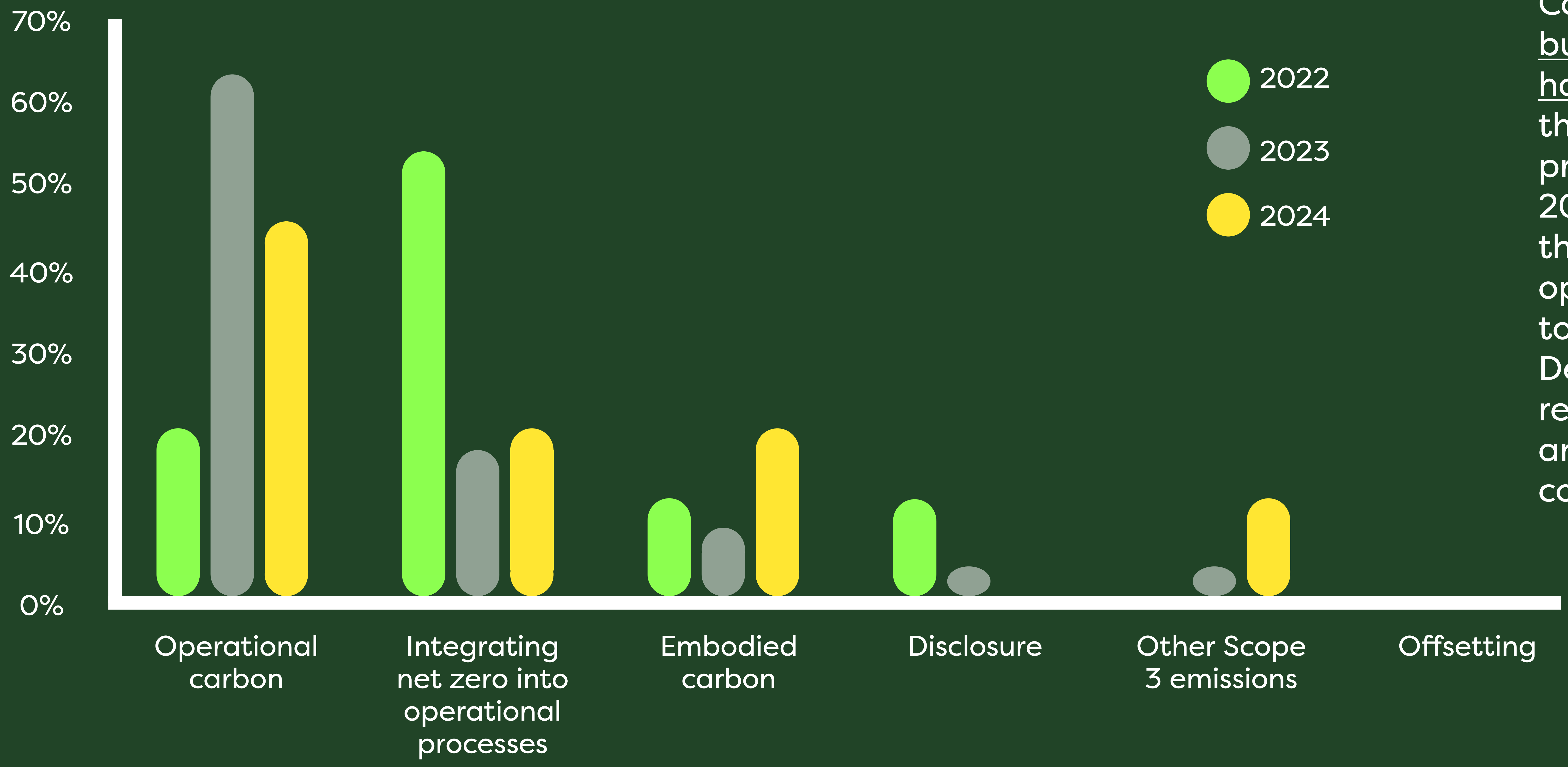
Meeting reporting requirements is the top priority

Those with responsibility for net zero in their business need to have an understanding of the climate disclosure legislation which sits alongside this. Mandatory requirements need to be met in order to avoid the penalty of hefty fines and accusations of greenwash, so it's no surprise that meeting reporting requirements is the top ESG priority in our survey.

Our net zero glossary is a useful reference point for all the net zero terms you need to know.

Net zero glossary

Net zero priorities



Operational carbon emissions continue to top the priority list.

Asset-level plans are the next step.

Considering that over half of the world's buildings that will be operational in 2050 have already been built,[2] it's unsurprising that operational carbon remains the highest priority for our respondents as we go into 2024. As the market matures, organisations that have set top-down corporate targets for operational carbon are beginning to progress to making asset-level decarbonisation plans. Developing these asset-level strategies requires a deeper dive into site-specific data, and for many organisations information gaps continue to challenge progress in this area.

Net zero priorities

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Offsetting continues to fly under the radar but will need consideration

Offsetting was notable in its absence. True to the fundamental principle of net zero carbon, it's encouraging that respondents have put an emphasis on reducing emissions rather than offsetting them. However, most of our respondents are working on the cutting edge of the industry and the absence of this area of net zero as a priority cannot be taken too literally. Current projections suggest it will not be possible to bring emissions from buildings to absolute zero by 2050 without any offsetting, so the need for robust offsetting strategies will increase. Many actors are reviewing their approaches to offsetting, often triggered by concerns of greenwashing and reputational risk arising from weak offsetting strategies, particularly given the wide discrediting of many offsetting schemes in 2023[3]

Progress made in integrating net zero into operational processes

In last year's survey, over half of our respondents said that integrating net zero into operational processes was their top priority over 2022 and looking ahead to 2023. This year, only 21% put it top. This suggests that progress has been made over the past year towards making net zero concerns an integral part of how their organisations work, factoring in carbon to processes of procurement, acquisition, and the monitoring and reporting of asset performance. This has perhaps freed up ESG teams to focus on ways to reduce emissions from the day-to-day operation of the assets themselves.

Scope 3 and embodied carbon on the rise

Scope 3 includes emissions from investments, tenant refrigerants, and purchased goods and services. Considerations of embodied carbon and other scope 3 emissions are starting to gain greater traction as regulations and voluntary disclosures become more standardised and embedded into business-as-usual. Emissions reporting frameworks are increasingly emphasising the importance of Scope 3 emissions. As organisations see progress in reducing their Scope 1 and 2 footprints, Scope 3 will become increasingly material.

Net zero drivers

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01. Increasing occupier / investor / public sentiment towards low carbon altenatives

02. Mandatory disclosures at asset level

03. Disclosures at fund / corporate level

Verco insights

To best support the industry in reaching net zero we also need to understand the underlying motivations that drive the priorities and the challenges organisations face in addressing them. The biggest drivers for net zero carbon for our respondents were mandatory disclosures and increasing sentiment towards net zero among occupiers, investors and the public. This indicates that actions toward net zero are not purely motivated by meeting compulsory standards; the sentiments of a business' stakeholders and their wider reputation are also important. This is encouraging, as it indicates that progress towards net zero is not completely reliant on government action and will also be driven by the market.

Net zero barrier 1: Budget constraints

The biggest barrier to decarbonisation identified by our respondents was budget constraints. However, buy-in from shareholders, boards, and investors was consistently low-ranking.

Perhaps although there is an appetite for sustainability strategies, there is still a lack of incentive to financially support them. Alternatively, the lack of resources to spend on net zero may reflect a broader context of a challenging economic climate in which budgets are squeezed more generally.

Verco insights

More evidence that sustainability measures can be directly translated into economic benefits would support the net zero agenda.

Investors and boards need confidence that it is worth spending money on better data solutions or swapping out gas boilers for heat pumps as they navigate difficult decisions in which they must balance the short term (often monthly or quarterly) performance of the fund against the long-term need to manage stranding risk and protect asset value.

Net zero barrier 2: Political uncertainty

Many actors in the private sector recognise that for an effective and just transition to occur, regulation must compliment market shifts toward a more sustainable future and without this external pressure, certain industries and businesses may not be as compelled to set robust transition plans. An uncertain political environment has therefore been flagged as a particular barrier to the transition. This feedback comes following recent concerns of the politicisation of the UK Government's climate ambition, where many organisations operating in the private sector have already expressed concern with the uncertainty of the future of the net zero agenda in light of the Government's recent steps that appear to go against the principles of the Paris Agreement.

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Verco insights

Many of our respondents emphasised the importance of mandatory disclosures in driving the net zero transition. For mandatory disclosures to be truly effective, we need a consistent framework to define the requirements of a 'useful' disclosure across all geographies. In the context of political uncertainty, such a shift is being driven by the private sector, rather than relying on governments to lead the way.

Net zero barrier 3: Collating accurate data

A lack of good quality data poses issues for meeting reporting requirements but is also a significant barrier to sustainability actions and strategies; fund/property managers and ESG teams without clear visibility on the performance of their assets will struggle to take the steps required to improve them. The challenge of data collection often arises when occupiers procure their own utilities directly.

One key strategy for overcoming this challenge is technology. Although increasing software capabilities was the lowest-ranked driver amongst our respondents, we believe the right software solutions can be transformative, facilitating positive data-sharing relationships with occupiers as well as simplifying the overall analytical experience. Collaboration with occupiers can also be enhanced through engagement programmes, which we have found greatly benefit the ESG goals of real estate managers. Even so, getting accurate data is not always possible, and in these cases, robust methods for filling gaps in data are needed.

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Verco insights

Finding data solutions is a key challenge to overcome, as it can unlock investor confidence[4] and provide a strong foundation for decision making. But even as we make steps to improve data, we can still make progress towards net zero, as the fundamental transitions we need to make are already known; Minimise scope 1 emissions, reduce energy demand and increase renewable energy procurement and capacity.

How Verco can help

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At Verco, our technical experts focus on supporting our clients in three key ways;

1. Providing strategic advice to help navigate the constantly shifting market and political landscape.

2. Delivering data and reporting solutions to comply with both mandatory and voluntary standards.

3. Conducting asset-level performance reviews with recommendations to inform future investment plans.

Find out more

We are committed to address the challenges and utilise the drivers described above to help facilitate sustainable growth. Over the next year, we will respond to the developing needs of the market with a range of key service areas to support our clients:

Developing actionable transition plans that consider whole life carbon

Overcoming challenges posed by a lack of data whilst aligning with new reporting regulations

Engaging with occupiers and the wider supply chain to improve data streams and emission reduction policies

Developing programmatic implementation strategies for audit recommendations

Verco's perspective

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Our survey reflects our experience; that net zero continues to be a key priority for real estate actors, even when they face tough decisions between short term performance and managing longer term risk or value potential. Practical challenges around the lack of credible ESG data and insights still hamper investor confidence and the lack of regulatory certainty adds to the challenge. Yet, the imperative to act continues to drive increasingly mature net zero transformation strategies across our client base and we look forward to tackling the next phase of the journey together.

Andries van der Walt - Head of Real Estate

A lot happened in 2023, with both progress and setbacks in the climate change agenda. As politicians continue to fall short in delivering on the requirements for a low carbon future, corporate entities must step up in 2024 and utilise the existing drivers to build the business case around their sustainability strategies. The transition to a low-carbon built environment will not be linear or smooth and we can see challenges in the road ahead. But momentum is building fast, with delivery programmes accelerating and focus points/barriers being more clearly identified. We look forward to what the coming year will bring.

Dave Worthington - Managing Director

References

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Links:

1 - United Nations Climate Change website - Global Stocktake description

2 - World Green Building Council website - The Problem with Net Zero Existing Buildings article

3 - The Guardian website - Revealed: top carbon offset projects may not cut planet - heating emissions article

4 - PwC website - PwC 2023 Global Investor Survey press release

Glossary of acronyms:

SEC CRD
Security and Exchange Commission's (US) Climate-Related Disclosure rules

CRREM
Carbon Risk Real Estate Monitor

SBTi
Science-based Targets Initiative

PCAF
Partnership for Carbon Accounting Financials

WGBC
World Green Building Council

CSRD
EU's Corporate Sustainability Reporting Directive

FCA SDR
Financial Conduct Authority's (UK) Sustainability Disclosure Requirements