



## ESG real estate insights

### Global perspectives on sustainability and climate

#### The sustainable (project) cashflow

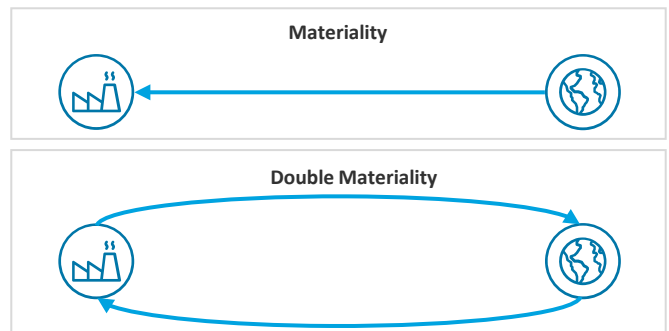
Green buildings, sustainable projects and sustainable communities are in high demand, and they often command higher property values. Intuitively, these last longer and do perform better with lesser need of resources. This implies that, whatever extra we spend in the phases of design and construction will be returned in the form of savings and positive ESG impacts in the phases of operation, and -here come circular economy- in the afterlife of the object.

Sustainability and efficiency are almost equivalent for real estate when it comes to assets: energy efficiency, sustainable materials, waste reduction, green livable spaces, circular economy, resilience to climate change and natural disasters, inclusivity and accessibility and other aspects that make a project ESG-compliant and consider its impact on local communities creating value by creating jobs and fostering economic activity.

All these aspects can directly transfer sustainability value into financial value for the project by projecting into the cashflow the environmental, social and governance (ESG) impacts of the project.

This is the base of the triple bottom line<sup>1</sup> theory, and the newly updated concept of double materiality.

**Figure 1: Materiality vs. Double Materiality**



Source: ['Double materiality': what is it and why does it matter? - Grantham Research Institute on climate change and the environment](#)

## Considerations towards the cashflow of the real estate project, does ESG actually increase the inflows (add value to the real assets)?

When creating a cashflow for a real estate project we consider outflows related to the real estate title acquisition, design and permitting, construction, and the operational costs but, we should also consider the afterlife of the objects and the sometimes/someplace/increasingly compulsory need to account for demolition and land remediation to return the estate (land) to the status prior to the development.

On the outflows, more sustainable objects are more efficient in the use of resources and have fewer operating expenses and maintenance costs. Also reducing potential penalties due to the lack of compliance with ESG-related regulations. Outflows related to energy cost could stabilize further when considering purchase power agreements (PPAs) which, with a certificate of origin from a renewable source, can also serve towards the decarbonization goals, thus meeting efficiency, sustainability, and risk objectives.

Insurance fees are another potential cost to cut as buildings and projects that incorporate resilient, adapted measures are better equipped to withstand natural disasters and climate change, reducing the risk of property damage and loss of income.<sup>2</sup>

On the inflows, “green” assets increase the capacity to generate income attracting environmentally conscious buyers and tenants willing to pay “green premiums” for properties that align with their values.<sup>3</sup> Tenant retention rates also improve in a healthier and more comfortable environment as tenants are more likely to renew their leases if they are satisfied with their living or working conditions.

EU Funds and governments’ financial incentives for implementing sustainability measures, such as tax credits or subsidies, should also be accounted for.

Finally, lenders may offer lower interest rates or preferential terms for sustainable projects, even activating capital that, without sufficient disclosure of ESG impacts, would never consider real estate assets as an investment class.<sup>4</sup>

However, there may be additional costs associated with obtaining certifications or meeting sustainability standards, which can increase the cost of financing.

Overall, the increased outflows accounted for in the design and construction phases will be easily outnumbered by the reduced operating costs in the operational phase leading to increased cash flows and higher net operating income, which will increase the value of the property.<sup>5</sup>

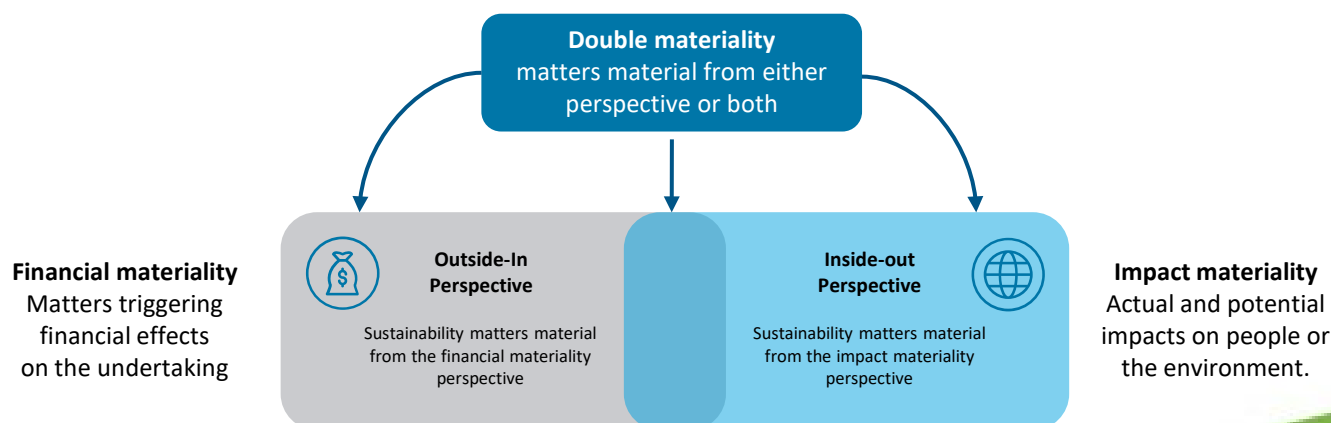
Companies that prioritize sustainability can enhance their brand image and attract environmentally conscious customers, investors, and employees. The “green” reputation of a company’s portfolio will create a positive brand image that will increase the goodwill value thus transferring direct value from the project to the company that promotes or owns the estate. This can translate into increased revenue and shareholder value, which can increase the value of the real asset.<sup>6</sup>

Even more value will kick in when/if divesting, with two components to consider: the increased net present value of the receivables and the residual value of the objects that can be increased by embedding circular economy solutions to all elements of the project: land plots being developed in a “reusable” way, construction and equipment elements being reusable or recyclable - modularity for circularity - to name the most evident. Everything to make the project more resilient and valuable by elongating the active life and capacity to produce income.

The value is perceived by all stakeholders in the value chain: workers, users, investors, communities, and suppliers. It is important to mention that “no action” is no longer an option: positive screening by conscious users and investors does activate “green premiums” and good reputation, at the same time we are already seeing negative screening imposing “brown discounts,” and even by rejecting projects that cannot show a minimum green value.

It is no longer about how much money you make but also about how do you make that much money.

Figure 2: Double materiality



Source: "Sustainability Reporting Guidelines", Deloitte, EBRD and Prague Stock exchange<sup>7</sup>

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## Endnotes:

1. Please read what the author formulated beyond and towards regeneration in [Elkington, John](#) (June 25, 2018). ["25 Years Ago I Coined the Phrase "Triple Bottom Line." Here's Why It's Time to Rethink It"](#). Harvard Business Review. Retrieved October 11, 2019.
2. The European Investment Bank (2019) highlighted the importance of resilience measures in real estate and infrastructure investments to reduce the risk of physical damage and loss of income from natural disasters. <https://www.eib.org/en/publications/investment-report-2019>. Also The Royal Institution of Chartered Surveyors has published various reports on the importance of building resilience to climate change in the real estate sector
3. The Green Building Council (2022) reported that buildings certified under the LEED program have shown a 4% increase in property value compared to non-certified buildings. <https://www.usgbc.org/articles/leed-builds-value-real-estate-investors-usgbc-los-angeles>. A study by The Bucharest University of Economics and the Vienna University of Economics and Business \*WU (2016) found that green-certified buildings had a 16% higher asset value than non-certified buildings. [https://www.researchgate.net/publication/299764597\\_Is\\_the\\_higher\\_value\\_of\\_green\\_buildings\\_reflected\\_in\\_current\\_valuation\\_practices](https://www.researchgate.net/publication/299764597_Is_the_higher_value_of_green_buildings_reflected_in_current_valuation_practices). The Journal of Real Estate Finance and Economics published an article (2022) establishing how real estate portfolios with a higher sustainability score achieved higher returns than those with lower scores. [https://www.researchgate.net/publication/361357146\\_Sustainability\\_and\\_Private\\_Equity\\_Real\\_Estate>Returns](https://www.researchgate.net/publication/361357146_Sustainability_and_Private_Equity_Real_Estate>Returns)
4. The International WELL Building Institute (2020) reported that buildings certified under the WELL Building Standard had higher tenant retention rates. A survey by the US Green Building Council (2018) found that 81% of tenants in LEED-certified buildings were satisfied with their indoor air quality, compared to 66% in non-certified buildings. [U.S. Green Building Council. \(2021\). Research Anthology of Health-Promoting Building Strategies.](#)
5. A study by the US Department of Energy (2012) found that green buildings had an average energy savings of 24% compared to non-green buildings. [https://www.eia.gov/consumption/commercial/data/2018/pdf/green\\_buildings\\_cbecs.pdf](https://www.eia.gov/consumption/commercial/data/2018/pdf/green_buildings_cbecs.pdf). The World Economic Forum (2021) reported that energy efficiency measures in buildings could reduce operating costs by 20-30%. <https://www.weforum.org/agenda/2021/02/why-the-buildings-of-the-future-are-key-to-an-efficient-energy-ecosystem/>
6. The World Economic Forum' Future of Work website continuously reports how companies that prioritize sustainability have higher employee satisfaction and are more attractive to investors. <https://www.weforum.org/agenda/future-of-work>. A study by Harvard Business Review (2016) found that companies with a strong environmental and social performance had a higher market value and financial performance. [Social-Impact Efforts That Create Real Value \(hbr.org\)](#)
7. <https://www2.deloitte.com/cz/en/pages/risk/topics/udrzitelny-rozvoj.html>

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