on point

Jones Lang LaSalle

CoreNet Global

Global Trends in Sustainable Real Estate: An Occupier's Perspective

2007 represented a tipping point in occupier attitudes towards sustainability. Momentum will gather further and faster in 2008.

A Jones Lang LaSalle / CoreNet Global survey of over 400 occupiers globally, identified that there is clear occupier demand for sustainable real estate solutions.

Occupiers are prepared to pay a premium to secure sustainable real estate but the ability of the supply side to provide sustainable solutions is currently viewed by occupiers as sporadic.

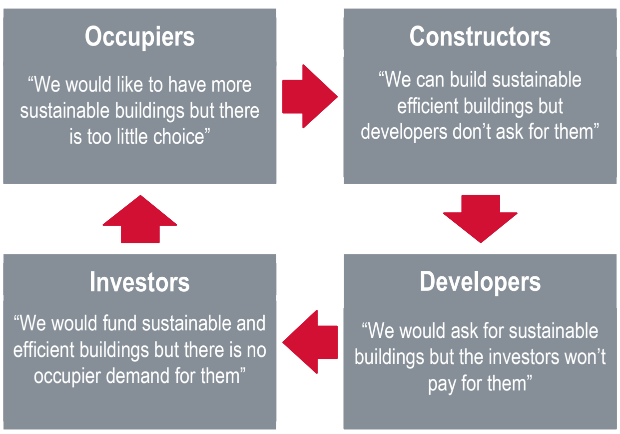
Introduction

Looking back, one theme resonates in the demand side of the property industry during 2007: sustainability. The year saw a steady growth of interest in and attention to the contribution of corporate real estate to sustainability and corporate social responsibility (CSR) commitments. As we enter 2008, most major corporates now have public sustainability statements. Against this back-drop they are also beginning to pursue sustainable solutions in both new and existing real estate portfolios.

Sustainability is thus firmly on the corporate agenda. But the views of corporate occupiers towards sustainable real estate are not widely known. This briefing paper addresses this by drawing upon the results obtained from a global survey of over 400 corporate occupiers, conducted jointly by Jones Lang LaSalle and CoreNet Global at CoreNet Summits in Singapore, Denver, Melbourne and London during 2007. The aim of the survey was to gauge corporate awareness, to understand the key issues driving sustainability in real estate, and to investigate some of the perceptions that may be shaping corporate action and therefore real estate demand.

The views expressed by occupiers and their advisers through this survey confirm that sustainability reached a tipping point in 2007. The corporate momentum behind sustainability and CSR will further intensify over the next twelve months and will generate real and consistent occupier demand for sustainable real estate across all markets. The ability of the supply side in these markets to address such demands is, as occupiers have identified, presently sporadic at best and needs to be urgently addressed.

Figure 1: The circle of blame.



These results provide a challenge to the cycle of blame (Figure 1) that has typically constrained the development of sustainable real estate solutions throughout the world. They contradict the notion that sustainable real estate is not commercially attractive to investors and developers on account of a paucity of occupier demand. There is pent up demand for sustainable real estate amongst major corporate occupiers globally, and those on the supply side that are able to present innovative and effective solutions are most likely to profit as the decade draws to a close.

3 Occupier Perspectives on Sustainable Real Estate

Three clear occupier views emerge across the globe. Although the strength of response varies from region to region, in general the same opinions and issues characterise corporate occupiers irrespective of geography.

1. Sustainability is not for tomorrow's agenda. It is a critical CRE issue right here, right now.

As Figure 2 shows, 47% of global respondents indicated that sustainability was already a critical issue to them, with a further quarter of all respondents maintaining that sustainability will become a critical issue to them over the short term, that is within two years.

There is however clear variance across the globe in the pace at which sustainability is becoming a critical Corporate Real Estate (CRE) issue (Table 1). EMEA is the region where the issue has taken strongest hold, most quickly. 60% of EMEA respondents regard sustainability as a critical issue now, compared with 50% of Australasian respondents. In contrast, in Asia-Pacific only 40% of respondents saw sustainability as being critical right now. Furthermore in Asia-Pacific even the short-term perspective was less evident than other global regions, with a quarter of all respondents seeing sustainability as being only a medium term (three to five year) issue.

Figure 2: Expectations as to when sustainability will become a critical business and CRE issue.

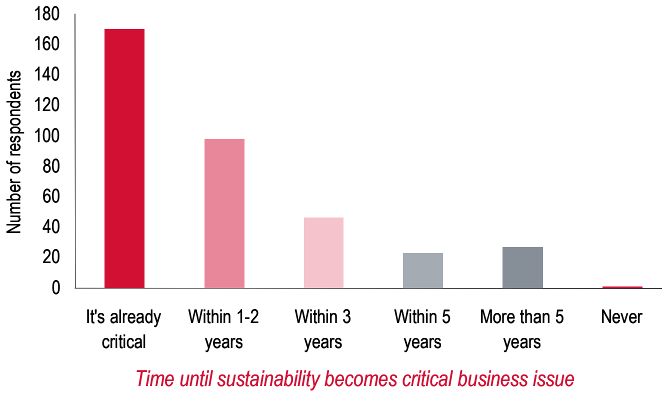


Table 1: When will sustainability be a critical business issue to corporate real estate?

	EMEA	North America	Asia-Pacific	Australasia
Critical Now	62%	44%	42%	52%
Critical within 1- 2 years	23%	35%	20%	23%

This is likely due to the diversity of property market cycles within the Asian-Pacific region and difference in sustainability drivers across these markets. In addition, the Asia Pacific survey was undertaken in March 2007, and sustainability is an issue that experienced significant growth in momentum throughout the year right across the region.

We are seeing a significant push towards sustainability in many countries in Asia Pacific. China, India and Singapore are three countries attempting to improve sustainable real estate development through revising standards and policies. In Singapore, the government is being able to drive sustainability effectively and strongly due to its small size and culture. While the more mature Singapore market is making in-roads in commercialising sustainability, there is nothing in Singapore equivalent in scale and scope to the major sustainable developments going on in China and India now. India has one of the first LEED rated buildings in Asia and Olympia Technology Park in Chennai, which has achieved a LEED Gold Rating, has been identified as the world's largest green building.[1] China is building the world's first eco-city in Dongtan, anticipated for completion in 2010. At the same time, there are also other large-scale sustainable developments entering the planning stage in China.

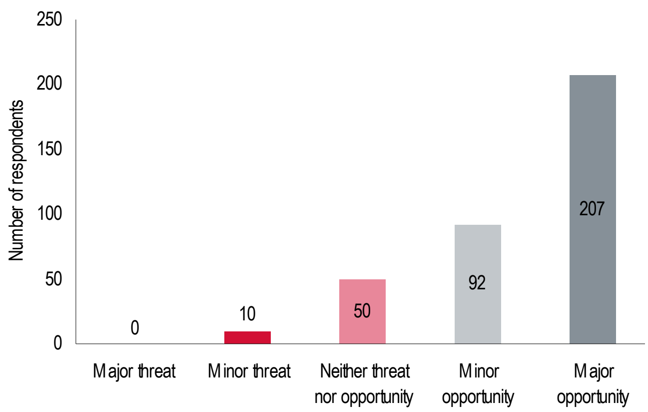
Those occupiers at the vanguard of sustainability are typically global in orientation and are appraised on a global basis. They are bringing demands for sustainable real estate to the fore across Asia. Developing markets have a significant opportunity to cater to these requirements by introducing sustainability initiatives in new buildings due to the higher level of new development compared to existing stock on the market.

Developing markets in Asia-Pacific have a real opportunity to implement sustainability initiatives as an integral part of a country's real estate development. This could ultimately lead to a higher level of sustainable stock available across the market. More mature markets will need to focus on implementing sustainability improvements in existing stock to cater for demand.

The urgent and critical focus upon sustainability is understandable when one considers the exposure that real estate represents to a corporate. Typically 50% of all energy and as much as a third of all water is consumed in commercial real estate, meaning that the performance of real estate has a direct and immediate impact on an occupier's ability to reduce its carbon footprint and environmental degradation.

Accordingly, in publicising their sustainability credentials and intentions public through CSR statements, occupiers have to prioritise the issues surrounding green real estate. It is little wonder therefore that the development of sustainable real estate is either critical or near critical for many of the world's leading occupiers. This trend will continue to intensify over the short to medium term particularly as initial trailblazers provide evidence of financial and non-financial out-performance through the adoption of clear sustainability strategies.

Figure 3: Sustainability – an organisational threat or opportunity?



Encouragingly, and as Figure 3 shows, occupiers regard issues surrounding sustainability as an opportunity rather than a threat. Occupiers in EMEA and Australasia are the most opportunistic, with 87% of respondents from each region regarding sustainability as an opportunity and more than 60% in both regions regarding the issue as a 'major opportunity'. Even in

[1] LEED is a Green Building Rating System developed by the US Green Building Council which provides a suite of standards for environmentally sustainable construction.

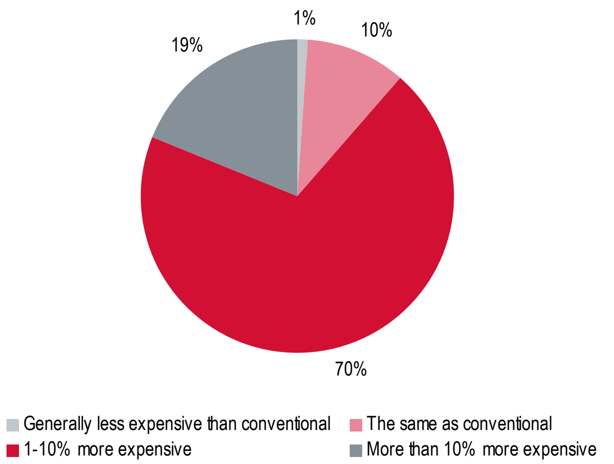
Asia-Pacific, which had the most mixed set of responses, 79% of all respondents saw sustainability as representing an opportunity with just over 50% seeing the opportunity as being a major one – albeit over a longer time period than their counterparts globally.

From a property perspective, sustainability offers a key opportunity for CRE executives to have increasing influence across their entire organisation. CRE will have a pivotal role in ensuring that company wide sustainability goals are achieved and in doing so will have a marked and direct impact on corporate financial performance.

2. Corporate occupiers accept that sustainable real estate costs more to deliver and are prepared to pay a premium.

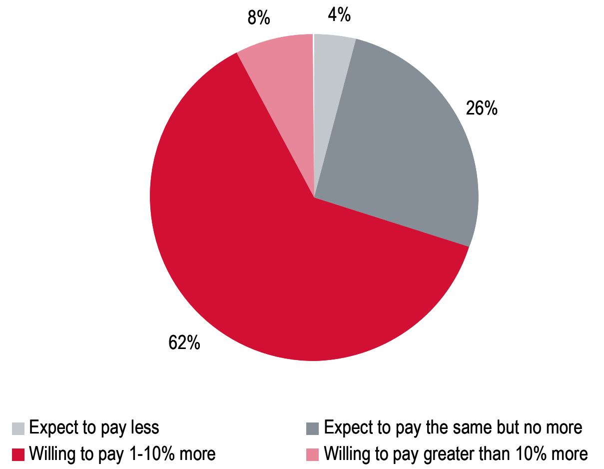
Our survey shows that occupiers are pragmatic in respect of the additional costs incurred by owners and developers in designing, delivering and certifying a building to BREEAM, LEED or equivalent standards.[2] As Figure 4 shows, 70% of respondents from EMEA and North America suggested that sustainable real estate costs up to 10% more than conventional product to bring to market. Indeed, a further one in five respondents maintained that the actual additional costs were in excess of 10%. Only 11% of total respondents argued that delivering sustainable real estate actually cost less or no more than conventional product.

Figure 4: Perceived additional costs of supplying sustainable real estate.



This acknowledgement of additional costs is particularly interesting in light of responses to questions related to the premium that corporates are prepared to pay in order to source a sustainable real estate solution (Figure 5). Again, 70% of survey respondents globally stated that they were prepared to pay a premium rental for sustainable real estate, 62% that this premium would be in the region of 1-10% more, and a further 8% stating that they would be prepared to pay a double digit premium for appropriate, sustainable solutions. In contrast, and critically, a quarter of respondents maintained that they were not prepared to pay any more for a sustainable solution, irrespective of their views on the costs of delivering such product to the market.

Figure 5: Premium that corporate occupiers are prepared to pay for sustainable real estate.



Again there are interesting regional variations in results. As Table 2 shows, the EMEA and Australasian regions show the most similar characteristics.

Table 2: How much more occupiers are willing to pay for sustainable real estate solutions, by region.

Premium	EMEA	North America	Asia-Pacific	Australasia
Same or less	34	23	36	32
1-10%	64	74	48	61
>10%	2	3	16	7

Two thirds of all respondents from these regions stated they were prepared to pay a premium for sustainable real estate solutions. In North America the picture is similar, but the proportion prepared to pay some kind of premium was actually higher – at 77%. It is clear from all three regions that a 1-10% premium is deemed appropriate by the occupier, with only a small number of respondents willing to pay in excess of 10%. In Asia-Pacific there was actually a higher number of respondents prepared to pay double digit premiums (16% of respondents) – possibly due to the market scarcity of solutions.

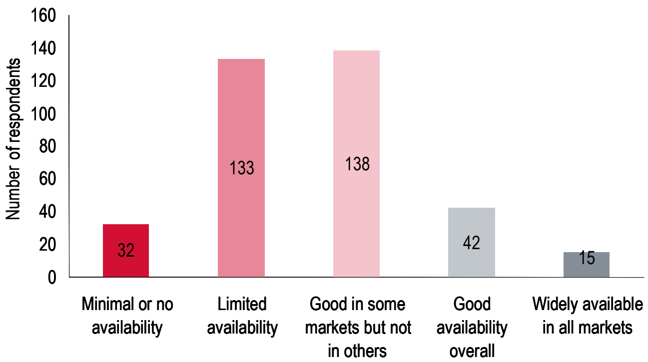
[2] BREEAM is an environmental assessment method for buildings. BREEAM assesses buildings against a set criteria and provides an overall score which will fall within a band providing either a pass, good, very good or excellent rating.

Across all regions such results do require some qualification however. Although many occupiers accept that a premium may need to be paid, it is more probable that as the sustainability issue becomes further embedded in markets across the globe, inefficient buildings or buildings that do not offer a suitably sustainable real estate solution may suffer a discount, with assets that can demonstrate leadership in this area commanding top rental levels. What the survey illustrates therefore is that not only is a pricing differential likely to develop but that issues of sustainability and efficiency are increasingly becoming part of the 'quality mix' that corporate occupiers look for when choosing Grade A real estate.

3. A good sustainable real estate solution these days is hard to find.

While the discussion around costs and the willingness to pay is encouraging, there is another problem regarding the availability of sustainable options in the market. When asked, only 17% of US respondents think there is good availability of sustainable real estate solutions within the US market. So, despite the willingness to pay the price, a lack of options and services in some areas had been a limiting factor. This is true of EMEA too with 93% saying that sustainable solutions are patchy or limited. Collectively, 46% of our global sample perceived no, minimal or limited availability of sustainable real estate solutions in the markets in which they operate. Of course, as the foot-print of corporates takes in more and more of the emerging markets, the ability to tap into sustainable real estate becomes ever more challenging (Figure 6).

Figure 6: Perceived availability of sustainable real estate solutions.



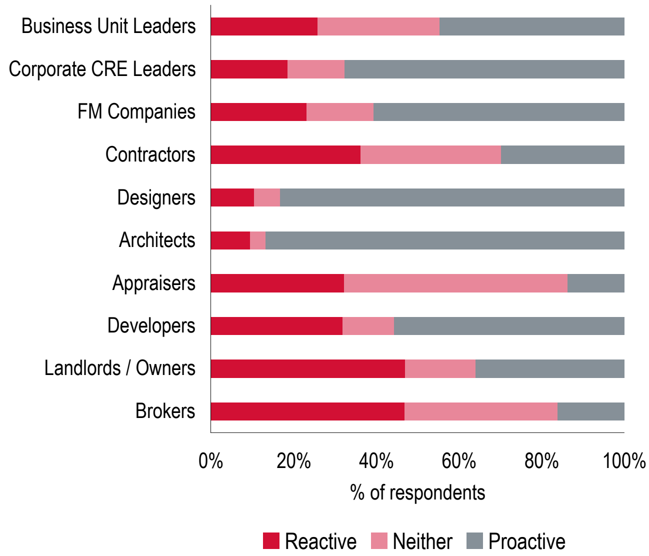
This trend represents both an opportunity and a threat to those on the supply side of the market. Occupiers are prepared to pay a premium for sustainable real estate, which means that by developing and owning such real estate, investors can look to future-proof investment portfolios. Additionally in some markets there is an opportunity to push up capital values by demonstrating the environmental credentials of real estate.

A shortage of stock means there is clearly also a market gap to fill: however, given the significant lead times for Grade A real estate there is a risk that those that do not move quickly enough to stay ahead of market sentiment may be left behind.

In the US, McGraw Hill, using USGBC data estimated that in 2006 2% of the US commercial real estate stock is currently LEED – so for occupiers sustainability is rarely on the menu. There are signs that a supply side response is emerging, however, as US office market development pipelines show an increasing proportion of new buildings are classified as LEED – with New York City and Atlanta having 80% of new pipeline classified as such and Boston and Chicago around 55%. This has been driven by a combination of regulations, incentives and tenant demand.

One reason for the lack of options is highlighted in another question we asked about how proactive the different stakeholders and service providers are about sustainability (Figure 6). Other than architects and designers, the perception is that the various elements of the real estate industry are not yet doing a good job in thinking and acting ahead of the need for sustainability. These responses are not where they need to be in order for the industry to advance sustainability. This will change rapidly given the critical regard that occupiers place on sustainability. In fact, other constituents not even on this list are jumping into the fray and getting smart about sustainability. Real estate investors, leaders and insurers, to name a few, have at least started to mobilise around the topic of sustainability and investigate new products and strategies as a way to grow, manage risk and diversify.

Figure 7: Perceived pro-activity of key property players.



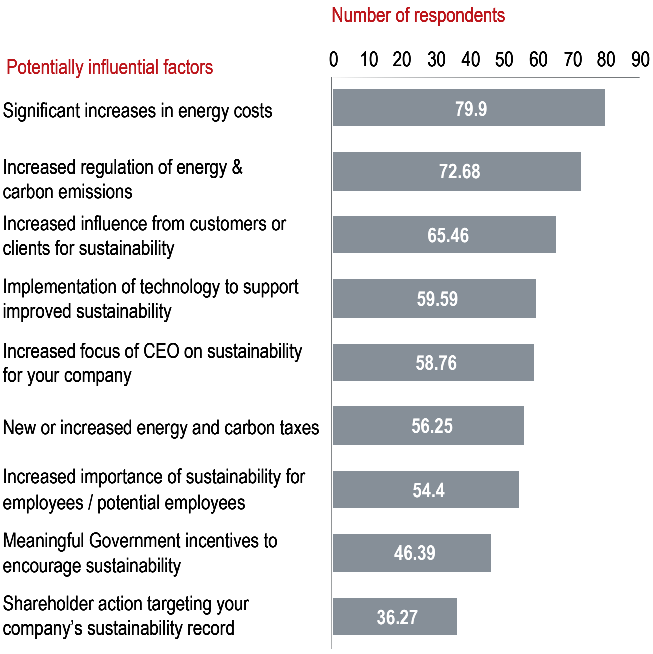
It is also evident from these results that within occupier organisations CRE leaders are seen as driving the sustainability agenda more proactively than many business unit leaders. Across the EMEA and North American surveys, 68% of respondents regarded CRE team leaders as being responsive about sustainability compared with 45% of business unit leaders. It would appear therefore that the ability to influence the wider corporate agenda has not been lost on CRE teams.

Where next?

It is clear from the results obtained both globally and regionally that sustainability issues have moved rapidly to the centre of occupier thinking and decision making. 2007 can thus be seen as a tipping point in corporate attitudes towards sustainability. It is within real estate that this strong interest is most likely to manifest itself as clear action. Greening the existing portfolio and sourcing sustainable real estate going forward represents both a tangible and increasingly measurable corporate effort to address the environmental impact of corporate occupiers.

It is inconceivable that the momentum that gathered during 2007 will be reversed. Instead we predict that interest and action will intensify over the next twelve months as occupiers seek increasingly innovative sustainable real estate solutions. Respondents to our survey identified a range of factors most likely to influence changing attitudes towards sustainability over the medium term. As Figure 8 illustrates, the future strength of occupier attitudes towards sustainability are heavily influenced by developments in terms of energy costs and regulations around energy and carbon emissions.

Figure 8: Factors that might influence future attitudes towards sustainability.



Interestingly, other specific environmental issues such as water utilisation and carbon emissions were ranked lower, and by a significant gap. This suggests that while the importance of corporate sustainability is increasing, not all of the details are yet in full focus and corporate occupiers may not be fully grasp how interdependent the components are in terms of their cumulative impact on the environment. The factor respondents identified as most likely to increase the importance of sustainability was again increasing energy costs. With energy utilisation ranking highly on the list of current priorities, and increasing energy costs seen as most likely in escalating the sustainability issue, corporates clearly recognise that sustainability can become a 'cost saving' technique on the energy front with a positive impact on the economic bottom line in addition to its environmental importance.

Other factors that companies indicate could increase the importance of sustainability included regulation, customer influence and employee interest. Companies are seeing the probability of regulatory changes (such as taxes or new reporting demands) impacting their business, so the risks of being unprepared for potential changes have increased beyond a marketing dilemma. The rise of employee interest in the topic is no surprise either. Companies see their real estate, corporate identity and values as critically important in attracting and retaining the labour that drives their businesses. In an increasingly challenging labour market, sustainability has and will become one of the ways companies can improve their competitive advantage in the often cut-throat war for talent, and further improve productivity and quality of the work environment once the talent is secured. Some early findings regarding the impact of sustainable space on employee health, productivity and job satisfaction are compelling. The young knowledge worker talent, in especially short supply, is particularly keen on environmental issues and corporate social responsibility.

Going forward, the question facing occupiers is no longer whether sustainable design should be considered or pursued in commercial real estate: rather it is how you justify choosing *not* to have sustainable real estate. Sustainability is not a passing fad – it is rapidly being mandated as a business imperative. Architects and engineers have been proactive on the topic for some time and we now see more service providers, real estate investors, lenders and insurers mobilise on the topic of sustainability and investigate new products and strategies as a way to grow, manage risk and diversify their businesses and real estate portfolios. As we enter 2008 one thing is for certain – the green wave of momentum will not dissipate, meaning that sustainability will be at the very forefront of occupiers' real estate decision making.

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