

# Impact Investing in Real Estate

## Returns with purpose

October 2019

Impact Investing, where positive contributions to society and the planet are delivered with the aim of achieving attractive returns, is the investment model advocated by Schroders. In today's world it's important to understand and develop an investment's social purpose as we believe it will help ensure resilient returns for the longer term.

This paper explores Impact Investing and where impact can be achieved in Real Estate.

### Introduction

Impact Investing should be considered central to real estate investment. The built environment supports people in every aspect of their lives – homes, workplace, health, education and leisure. Therefore focussing on the quality of internal and external environments will provide a direct benefit to people and society and deliver both occupiers' and landlords' expectations.

Buildings are reliant on resources and energy for construction, refurbishment, maintenance and operation, making it crucial to understand environmental impact, particularly carbon, through every stage of their lifecycle. However, as with other sectors, investors in real estate have not given enough consideration to the impact it has on people as well as the planet.

Today, in our world of social change and climate emergency, reducing negative impact and delivering positive impact to the planet and society is necessary to support our future and our investment horizons. Impact investing is therefore beyond ESG because it seeks to proactively take action to improve situations, doing good for society, the environment and providing the scope for attractive returns.

### What is Impact Investing?

Impact investment are investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return.

Impact investments can be made in both emerging and developed markets, and target a range of returns from below market to market rate, depending on investors' strategic goals.

Source: The Global Impact Investing Network 2019.

### Investors want Sustainable Investments

The majority of investors want sustainable investment options and people are interested in a broad range of social and environmental issues. Many have yet to recognise that their investment decisions enable them to personally contribute to a more sustainable society. The opportunity is therefore significant to present investment ideas that clearly set out and deliver on people's values enabling investment which supports society, the environment and meets investment ambitions.

Fund managers can influence companies' approaches to environmental and social issues. People care about a broad range of behaviours

Areas of importance to potential investors on a scale of 1 (not at all important) to 10 (extremely important)



Schroders' Global Investor Study 2018.

## Understanding Impact and Real Estate

### UN Sustainable Development Goals

In 2015 all United Nations Member States recognised the range of issues we all face by adopting the UN Sustainable Development Goals (SDGs) as part of the 2030 Agenda for Sustainable Development. These SDGs provide a common framework for public and private organisations to present the impacts of their activities and report on the outcomes they achieve.

The choice of SDGs an organisation makes is important. The selection should be mapped to an organisation's activities and purpose, therefore appropriately recognising the influence it can have, to ensure that positive impacts can be delivered and importantly that they are evident to all stakeholders.

### UN Sustainable Development Goals



Source UN 2015 Agenda for Sustainable Development.

## SDGs and Real Estate

The built environment supports people, business and communities and requires resources and energy to function. Therefore understanding potential contributions as well as the negative impact should be an inherent element. Opportunities for recognising and delivering impact within real estate are significant.

At Schroders we have identified three SDGs with significant potential for impact:

### SDG 8 Decent Work and Economic Growth

A real estate owner should consider the number of jobs a building enables, whether for construction, servicing or simply the company occupying the space and how these are local jobs, support education, training and skills and span age and advantage groups thus supporting communities and the economy.

### SDG 11 Sustainable Cities and Communities

The quality of the built environment is key to successful, safe, resilient and sustainable cities and communities. This is where all aspects of real estate fundamentals come together: architecture, streetscape, transport and connectivity, housing, landscaping, biodiversity and amenities. All aspects must respond to and evolve heritage and culture to foster places where the wellbeing of people, communities, business and nature thrive.

### SDG 13 Climate Action

Buildings are a significant contributor to carbon emissions, with 40% of global emissions commonly cited. At a portfolio level programmes should exist to reduce energy consumption and improve energy efficiency, use and install renewable energy as well as require informed choices for construction design, processes and materials to manage whole life carbon and conserve our natural resources. It is accepted we need to target net zero carbon for buildings, both for construction and operation, and the real estate industry needs to respond to this challenge.

### SDGs and Schroder Real Estate's Pillars of Impact

At Schroders we have taken these three SDGs to frame our pillars of real estate impact: People, Planet, Place and Prosperity. These provide a holistic view across social, environment and economic impacts together with investment returns forming the basis of our Real Estate strategy. We believe that purposefully considering our impacts should enable us to deliver better investment returns for the long term contributing to a better future for us, society and the planet.

## Schroder Real Estate's Pillars of Impact



## Delivering Impact in Real Estate

Impact can be achieved for all types of real estate, old and new, provided impact objectives are set at the outset. The extent of the impact will of course vary. The investment manager needs to recognise the contributions for each asset and how these can be managed to reduce negative and improve positive impact as an integral part of management strategy. Such an approach will involve giving greater thought and analysis of the occupants' physical, mental and wellbeing needs, supply chains, natural resources and materials, waste and landscape. Making impact an explicit consideration will support better management decisions and improve outcomes for all of a building's stakeholders as well as returns.



## Examples of real estate with impact in Schroders existing portfolios

### A regenerated town centre

Schroders has delivered a new town centre for Bracknell, a town in the South East of England. We have been invested in the centre for over 15 years and the new 54,000 square metre Lexicon Bracknell scheme opened in September 2017.

Unusually we have control over the majority of this town centre. The regeneration plan involved working closely with local government and the community to identify the needs of the centre and the town as a whole. The scheme involved delivering new retail, leisure and 1,000 homes as

well as renovating parts of the original retail, landscaping and public realm.

This collaboration helped shape the design and amenity of the scheme, including infrastructure and accessibility, and informed public safety and wellbeing. Apprenticeship and recruitment services were also developed to support the construction project, workers and staffing for new occupiers with around 3,500 new job opportunities created.

The scheme delivers a wholly regenerated town centre to position Bracknell as a significant retail centre in Berkshire. This should help attract further investment from the wider area to continue Bracknell's economic development and prosperity. As owners of the scheme we continue to invest in developing the town's future.

### Energy consumption and Renewables

Schroders is a signatory to RE100 and this commitment to 100% renewable electricity extends across our real estate portfolios. Our programme involves continual improvement in building operations and includes setting energy targets. For our UK portfolios we targeted a 6% consumption reduction over two years to 2018. Over the period we implemented a number of initiatives identified through asset audits including LED lighting, voltage optimisation and efficiency of heating, ventilation and air conditioning systems, supported by improvements to building management.

The programme achieved an 8.1% reduction which equates to 3.8m kWh, 930 tonnes CO2-equivalent avoided and a saving of £340,000.

### Socially and environmentally conscious Hotels

Across our European Hotels we are focussing on improving guest experience and supporting shared social and environmental values. We are working to remove single use plastic moving to microfiltered water instead of bottles, removing straws, cups and bathroom disposables and with our suppliers preferring loose goods instead of bagged. We are looking to local producers and donating unsold food products to schemes supporting those in need. We have an energy programme to reduce consumption and improve operational efficiency and use environmentally friendly cleaning products. Supporting our staff is vital to any hotel community, both front and back of house, across their needs to the roles they all contribute to ensuring our hotels consciously deliver on our values.

## Impact Investing and returns

Historically investors have perceived a trade off between creating social and environmental benefits and financial returns. It was accepted that you couldn't have both at the same time. Schroders believes impact investing is achievable with market returns. Schroders does not believe there needs to be a trade off between investment performance and environmental and social objectives.

Impact investment is about acting in a responsible and positive way; a core value for any business which rewards attractive returns and contributes to a better future for society and the planet for the long term. Responsibly considering our impact should be the model people, businesses and investors adopt to achieve change and address our climate and social crises and inequalities for all our futures.

### From ESG to Impact Investment



Source Schroders 2019.

## New Real Estate Sectors with Impact Opportunity

In addition to mainstream commercial real estate, we have identified two 'alternative' sectors which could deliver positive social impacts and attractive investment returns: social supported housing (SSH) and retirement living. Both sectors benefit the health and wellbeing of residents and provide wider benefits for their families, the local community and reduce the pressure on the NHS and social services. There is a shortage of good quality, modern space in both sectors and demand is set to grow, driven by long-term structural factors which are independent of the economic cycle. We expect both sectors to out-perform the UK commercial real estate market over the next five years with returns less correlated with the wider market, providing investors with some diversification. A summary of the opportunities is provided below.



### Social Supported Housing (SSH)

Positive Impact: Residents are some of the most vulnerable people in society.

- Transferring residents to new purpose built community settings has a positive impact on health and mental wellbeing. This frequently results in reduced life care requirements and costs to the state
- Providing such housing releases in-patient capacity for others with needs more appropriate to such settings
- Many adults with learning disabilities live with elderly parents. SSH provides a solution when parents can no longer provide care

Investment Case:

- The demand for SSH units is expected to increase as medical advances improve survival rates at birth and increase life expectancy
- There is a serious shortage of social housing stock
- SSH units offer significant cost savings to the government compared with registered care homes and in-patient hospitals
- Leases are 25 years to housing associations with inflation linked rents. Care and support are covered by separate arrangements, which means that residents (or their families) can change their care without moving home



families and unblock the local supply of family homes

Investment Case:

- Retirement living market is fundamentally undersupplied
- The UK has a relatively large proportion of wealthy older 65s, many of which are looking to downsize
- The UK over 65s population will account for almost all of the growth in the UK's population over the next decade
- The older generation is increasingly looking for a different housing offer to suit their lives

These sectors demonstrate how it should be possible to deliver positive social impact aiming for attractive risk-adjusted investment returns.

Impact investing, doing the right thing for us all, society and the planet, can provide long term sustainable and resilient returns. It is clear this should be the model for investors to adopt.

### Retirement Living

Positive Impact: Improved health for older people and the release of family homes in the housing market.

- Many older people live alone and suffer from chronic loneliness. Residents in retirement communities have improved mental health and tend to stay fitter and healthier than other people of a similar age. This also helps to alleviate the burden on local health and social services
- Residents' future care needs are provided for, reducing stress on them and their families
- By enabling older people to downsize, retirement communities allow them to give capital to their

## Conclusion

- **Impact investing is where positive social and/or environmental impact targets are set alongside financial ones**
- **We believe all organisations need to demonstrate how their activities make a contribution, to define and deliver their social purpose to support sustainable and resilient investment opportunities and returns for the long term**
- **Organisations are defining their social and environmental impacts with reference to the UN Sustainable Development Goals to recognise the influence and impact of their business**
- **Impact investing is the model to support a healthy society, the environment, economies, and investment returns for the future**
- **Positive Impact opportunities for real estate investors can be realised in existing portfolios and in new sectors, e.g. retirement living and social supported housing**
- **We believe returns do not need to be sacrificed to undertake Impact investment**

## In focus

### Risk Considerations

**The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.**

**Concentrated investments into the Real Estate sector may result in large changes in the value of the investments, both up or down, which could adversely impact your investment.**

**In difficult market conditions, it may be difficult to sell a security for full value or at all, therefore creating liquidity risk**

### Schroders Real Estate Investment Management

#### About our business

*Schroders has managed real estate since 1971 and is one of Europe's largest managers of real estate. Our investment range allows our clients to access real estate through open ended funds, listed REITs, specialist funds, joint ventures, separate accounts and global real estate securities. As at 30 June 2019, Schroder Real Estate manages £16.2bn of real estate on behalf of a wide range of institutions.*

#### Our philosophy

*Our philosophy is centred on consistent principles, to invest in strong fundamentals and to actively manage real estate portfolios. Our research-led approach identifies themes and trends informing our strategies to invest in locations and assets best suited to long-term real estate investment. As a result, our portfolios are located in 'Winning Cities' and regions best suited to benefit from these trends. We are an active manager of real estate, each asset has an individual business plan and is actively managed throughout its life to generate the optimum return for our investors.*

#### Sustainability

*We understand the importance and benefits of a sustainable approach to real estate investment. Sustainable investment considering Environmental, Social and Governance (ESG) is central to our investment approach and is integrated into the investment decision-making processes and business plans for all our investments.*

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