Clean Growth Strategy
Winter 2017

On 12 October 2017, Greg Clark, the Business and Energy Secretary presented to parliament the UK 'Clean Growth Strategy'. The strategy provides the UK's roadmap to de-carbonisation as a critical component of economic growth.

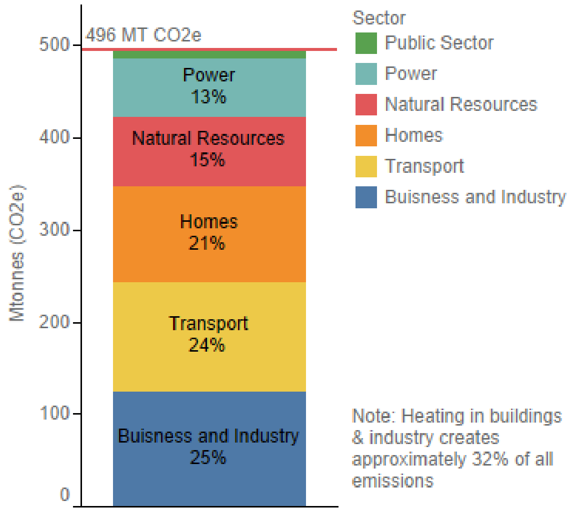
DTZ Investors has taken the opportunity to critically review the strategy and its alignment to the UK property sector.

The strategy sets out that clean growth is to be achieved through significant investment into the innovation of energy efficient technologies (£2.5 billion between 2015 – 2021) and importantly from the review, development and reform of UK policy and legislation.

'Clean growth' – Increasing economic growth while decreasing carbon emissions'

Background

The UK Clean Growth Strategy was developed in response to the Climate Change Act (CCA) 2008. The CCA commits the UK to reducing carbon emissions ≈80% by 2050 when compared to a 1990 baseline. To ensure that the UK keeps on track, 5 year caps on carbon emissions were instated, termed 'Carbon Budgets'. The UK Clean Growth Strategy sets out how the Government intends to meet the UK's fourth and fifth carbon budgets which should see carbon emissions cut to 57% below 1990 levels by 2032.



UK emissions by sector 2015, *source: https://www.gov.uk/government/publications/clean-growth-strategy*

What does this mean for the UK's property sector?

The 165-page strategy presents ≈50 proposals and plans across UK industry with several that will have a direct impact on the UK property sector. The proposals outline how improvements in energy efficiency of both domestic and commercial property will be met through the tightening of energy efficiency standards, and the raising of minimum standards. The Government propose to hold public consultation on the detail outlined in the strategy over the course of 2018.

With the tightening of standards, improvements in energy efficiency technologies and increasing expectations from tenants, the Clean Growth Strategy presents a clear business opportunity to improve returns and future-proof the value of real estate investments. DTZ Investors recognise that efficient assets incur lower operating costs, are more likely to achieve top market rents, and meet the increasing demand from occupiers for assets to support employee productivity.

In addition, within property investment and fund management of real estate portfolios, there is already pressure from the UN's 'Principles for Responsible Investment' to consider and invest in accordance with Environmental, Social and Governance (ESG) criteria.

DTZ Investors has been awarded an A rating by the United Nations Principles for Responsible Investment (UN PRI) for its commitment and approach to sustainable investment' - see here.

The Clean Growth Strategy sets to support this direction further, enabling funds to meet their obligations to reduce carbon emissions through the Government's investment in industry and technology. At an asset level, this translates to an increase in pressure for investors and fund managers to invest in the implementation of energy efficient building technologies, improvement in understanding of building performance and responding to changing occupier expectations. This will ultimately all lead to a raising standard of the UK's building stock.

Legislative Changes

The following presents current and future legislation that is likely to affect the commercial property sector once consultations are concluded:

1. Minimum Energy Efficiency Standard (MEES)

At 1st April 2018, the Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015 brings into force the first phase of the Minimum Energy Efficiency Standards (MEES) in the residential and commercial rented sector.

To bolster these regulations in spring 2018, the Government intends to hold a consultation on how best to improve the energy performance of commercial property through the tightening of MEES. The consultation will cover how Energy Performance Certificates (EPCs) can be improved across the wider industry considering recent improvements in technology, assessment frameworks, and data collection capabilities.

Reviewing the proposals, it is considered likely the consultation will conclude in the raising of the MEES minimum standard threshold, encouraging further improvement across the UK's building stock and impacting an increased breadth of transactions in the market.

In preparation for the Minimum Energy Efficiency Standards and the initial compliance deadline of 1st April 2018, DTZ Investors has undertaken an assessment of the risk associated across all properties via site surveys and enhanced Energy Performance Certificates, including due diligence at acquisition. Through this, DTZ Investors has been able to confidently map risk at a unit level with tailored risk plans to mitigate all F-G rated units from legislative risk.

As a side note, the EPC requirements derive from the EU's Energy Performance of Buildings Directive, therefore any future changes will be considered in the context of the UK only, outside of the European Union.

2. Building Regulations

The Government has commissioned an independent review of Building Regulations and fire safety, to be published in Spring 2018. Subject to the conclusions of that review, the Government intends to consult on making improvements to the current Building Regulations to further promote low carbon and higher energy efficiency heating, ventilation and air conditioning systems in new commercial buildings.

This is very likely to stimulate opportunities for developers to meet building regulations through the implementation of sustainable design practices and new technologies.

DTZ Investors ensures that external contractors in refurbishment and redevelopment projects adhere to our refurbishment policy, ensuring a standardised approach to driving asset performance and managing energy risks across the portfolio.

Providing guidance at this stage of the property life cycle ensures our buildings are efficient assets for our occupiers, and futureproofs the building stock as legislation evolves.

3. The CRC Energy Efficiency Scheme

In March 2016, the Government announced that it would dissolve the CRC scheme following the end of the 2018-19 compliance year. The Clean Growth strategy re-confirms this, alongside confirmation that the Climate Change Levy (administered by suppliers) is to increase from 2019 to meet the deficit from CRC.

This will streamline the business energy tax landscape by moving to a system where businesses are only charged one energy tax.

4. Streamlined Energy and Carbon Reporting Framework

The Department for Business, Energy and Industrial Strategy (BEIS) is seeking consultation on the proposal for Streamlined Energy and Carbon Reporting within the Companies Act 2006 business reporting framework. This is viewed as an excellent opportunity to align existing reporting frameworks to encourage greater transparency, and ensure disclosure of standardised comparable information, as outlined in the Bank of England's recently published recommendations on Climate-Related Financial Disclosures (TCFD).

5. The Energy Savings Opportunity Scheme (ESOS)

ESOS is a mandatory energy assessment for qualifying organisations. It was initially implemented in 2014 (Phase 1) under Article 8 of the EU Energy Efficiency Directive.

Qualifying organisations are required to undertake audits of the energy used by their buildings, industrial processes and transport to identify cost-effective energy saving measures.

Currently ESOS is in Phase 2 with a compliance deadline on 5th December 2019.

Under the Clean Growth Strategy, the Government is set to build on the existing scheme, undertaking an assessment of its effectiveness and considering any future reforms.

Energy Efficiency and Infrastructure

Between 2015 - 2021 the Government plans to invest £2.5 billion in the innovation of low carbon technology, driving a high growth and high value 'low carbon' sector of the UK economy. Investment is largely being put into the development of onshore and offshore wind, improvements in building efficiency and low emission transport infrastructure.

The strategy importantly recognises the necessity to drive down the cost of new green technologies to encourage adoption. To support this, the Government is providing £9.2 million for an Industrial Energy Efficiency Accelerator, that sets to provide companies the capital to implement innovative new energy efficiency technologies to boost operational efficiency.

The investment in industry and technology and the raising of minimum standards in energy efficiency is likely to improve the affordability of innovative green technology in the property sector; promoting sustainable property design and adoption of low carbon and higher energy efficiency heating, ventilation and air conditioning systems.

DTZ Investors takes a pro-active approach to property management through its Responsible Property Investment (RPI) programme, incorporating sustainability throughout the property management cycle including acquisition due diligence and occupier engagement which encourages the adoption of energy efficient practices throughout each property's life cycle.

For its discretionary managed portfolios, DTZ Investors has developed asset improvement plans, identifying opportunities to implement energy saving measures across its portfolios.

This process has so far identified over £300k of energy efficiency improvement projects with an average project payback of 4-5 years.

We continue to identify and implement these measures across our assets, ensuring they are fully integrated with our Planned Preventative Maintenance (PPM) programmes.

Conclusion

It is encouraging to see that the Clean Growth Strategy aims to reduce carbon emissions in the UK property sector and that clean growth is at the forefront of policy and economic decisions made by the Government. This is underpinned by a focus on technology innovation, incentivising uptake of low carbon technologies across the existing building stock and new developments.

The legislative improvements and investment in energy efficiency will be of importance for discretionary managed portfolios to improve returns and future-proof the value of real estate investments in both new and old properties, encouraging pro-active management practices, collaboratively working with on-site teams, property managers and occupiers to ensure that over time both investors and tenants benefit.

As a final note, it must be recognised that many of the proposed changes are subject to extensive consultation. However, it is a step in the right direction of a sustainable future and it is safe to say that this strategy lays the foundation to significantly impact future policy and legislation.

The full strategy can be found at here.

DTZ Investors supports Government investment in a low carbon economy and its plan to ensure the UK has efficient, long-lasting building stock. The DTZ Investors RPI Committee recognises the importance of seeking to minimise environmental impact and adopting a sustainable approach across all business activities and integrating these principles into the investment management process to manage portfolios in a cost effective and responsible manner. This includes protecting our funds against a changing legislative landscape whilst enhancing fund and asset performance for investors and occupiers.

For more information on DTZ Investors' approach to RPI, our policy can be found here.

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About DTZ Investors
DTZ Investors is a full service, vertically integrated, real estate investment and asset manager. Features of our core service include investment strategy advice, deal sourcing and underwriting, financial structuring, ongoing asset management and property management, regular portfolio review to assess risk, and client reporting. DTZ Investment Management is authorised and regulated by the Financial Conduct Authority. Registered in England no. 4633215. Registered Office: 85 King William Street, London EC4N 7BL.

Important Notice

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