Unlocking opportunities:

The power of robust ESG data

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AREF and the Aztec Group's recent research report, "Real estate fund operations of tomorrow", asked real estate CFOs and COOs what their investors had been most vocal or concerned about over the last 12 months. It won't come as a surprise to anyone reading this article that ESG topped the list.

Today's investors care about much more than just performance. They not only want a return, but a return that has been generated in a responsible, sustainable way. And, understandably, they want their investment manager to prove it – with data.

But the need for data doesn't start and end with investors. Regulators now demand it and investment managers have also woken up to the power of data to drive informed investment decision making. ESG data is now for the many, not the few.

This article, developed in partnership with JLL, shines a light on the world of ESG data in the field of real estate investment management, exploring current practices, the regulatory landscape, emerging trends and, perhaps most importantly, how fund managers can ensure they are well placed to capitalise on the power of robust ESG data.

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What we'll cover in this guide:

ESG data in action

The factors driving data collection

ESG data collected by real estate investment managers typically covers a range of qualitative and quantitative datasets created for a multiplicity of uses at corporate-level, fund/portfolio-level and asset-level. These uses all broadly map to just four interlinked drivers or ultimate purposes of this data, namely:

Legislative compliance

Reputation enhancement

Value creation

Risk mitigation

Practical examples of ESG data collection and analysis in line with these drivers include:

- Gathering electricity and gas consumption data to track the energy efficiency of buildings and reduce the carbon footprints of portfolios over time to meet legislative requirements;
- The evaluation of physical climate risk to assets, in order to mitigate the risk to capital value through damage, void risk and long-term obsolescence;
- Ensuring both compliance and good practice through improving health and wellbeing statistics on both construction sites and in operational buildings; and
- Tracking D&I statistics at the real estate fund manager itself to improve governance, and enhance reputation in the eyes of employees.

There is a real drive to understand the real impact of assets, portfolios and overall organisations on environmental and social challenges, and vice versa. Data is key to achieving this, enabling fund managers to make informed decisions on where to invest and what to avoid in line with the four drivers.

How ESG data is being used by fund managers

ESG data typically flows into four categories of use: 1) Legislative requirements; 2) Voluntary benchmarks and ratings; 3) Voluntary reporting against global strategic frameworks and guidelines; and 4) Internal reporting for decision-making purposes. Here's a summary of each:

1 Legislative requirements to disclose at corporate and fund level

a. UK regulations already require the annual reports of listed UK-based companies to include a table of greenhouse gas emissions for the past two years linked to a suitable intensity measure and a narrative of energy efficiency actions undertaken; and the Companies Act requires an evaluation of the company's impact on and regard for its stakeholders in any activities undertaken.

b. Climate risk management disclosures will be required from 2022. TCFD* (the Task Force on Climate-related Financial Disclosures) has created a set of guidance for organisations to report against in order to ensure investors have access to investment relevant climate risk information in a standardised format. The guidance specifies details to be provided around business strategy, governance and risk management, scenario analysis and portfolio assessments and the detailed performance data and targets at portfolio level.

c. In Europe, new regulations have been issued by the Commission which came into force, in part, in 2021 and will continue to be rolled out in 2022 – known as the Sustainable Finance Disclosure Regulation (SFDR) and the linked Taxonomy Regulations. The SFDR imposes mandatory ESG disclosure obligations for asset managers**, aiming to level the playing field on transparency in relation to sustainability risks, the consideration of adverse sustainability impacts in their investment processes and the provision of sustainability-related information with respect to financial products. The SFDR requires asset managers to provide standardised disclosures on how ESG factors are integrated at both an entity and product level, which are to be available via websites, in prospectuses and in regular reports.

2 Voluntary benchmarks and ratings assessing corporate or portfolio-level performance

These are used by investors to help decide which listed real estate companies or funds, or unlisted real estate managers, to invest with. Although voluntary, there is a significant amount of peer pressure and investor pressure to participate in these, and so they have become a market expectation, and do drive performance improvements as they evolve each year. Major players include:

a. The Global Real Estate ESG Benchmark (GRESB) is the most well-known annual sustainability assessment process for the global real estate sector, established in 2010; in 2021 more than 1,500 property companies, REITs, funds and developers participated, representing $5.7 trillion in assets under management, with the assessment covering nearly 117,000 assets across 66 countries. The survey questions run the gamut of social, environmental and governance policies through to the level of environmental performance data collection and the implementation of technical improvement measures across each portfolio submitted for evaluation. Via the GRESB portal, both listed real estate companies and unlisted funds submit detailed responses and evidence to a lengthy survey and upload a database of asset-level information. GRESB provides a list of all the categories of indicators that it gathers data against, which can be a really helpful first step to understand the nature of the ESG data required now within the real estate sector.

b. The UN Principles of Responsible Investment are also well-known in the investment industry, running the largest annual global reporting project on responsible investment activities and performance, albeit with a shorter track record of disclosure requirements for signatories than other sustainability reporting initiatives such as CDP (for listed companies and cities) or GRESB.

c. The major ESG index providers are MSCI, FTSE and S&P Dow Jones. The Dow Jones Sustainability Indices, the MSCI ESG and FTSE4Good series are all well known, and again give ratings on the ESG policies and performance of listed real estate companies. Their analysts will assess companies usually annually, sometimes via direct engagement, sometimes purely

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through the information available to them in the public domain – hence the importance of providing as much investment-relevant ESG performance data as possible via sustainability or annual reports. There are also a range of other independent ESG ratings providers.

3 Voluntary reporting against global strategic frameworks and guidelines

These are typically used by companies wishing to demonstrate best practice at corporate-level for reputational benefit:

a. The UN Sustainable Development Goals and their sub-targets allow organisations to assess their strategic intention, provide high standards to consider their long-term strategies and action plans against and to understand what data to, therefore, collect to be able to demonstrate progress.

b. The Global Reporting Initiative has been long-established and lays out by sector (including real estate) a set of best practice sustainability reporting guidance and recommended indicators.

c. Finally, EPRA and INREV are well-known organisations with voluntary environmental and social data reporting guidelines (the Sustainability Best Practices Recommendations - sBPRs, and Sustainability Reporting Guidelines respectively) – each have a set of detailed numeric sustainability KPIs which are reported on in tabulated form by listed companies and unlisted funds respectively, and performance assessed in an annual awards process.

4 Internal reporting for decision-making purposes

For example, a real estate fund manager might collate EPC ratings or undertake climate risk assessments across their fund. This would be done in order to decide which assets to retain and improve and which assets to sell – either because they are high-performing and currently commanding a premium, or there is a short window of opportunity before the market starts pricing in the risk burden they carry.

*See appendix 1 for TCFD recommendations.

**See Appendix 2 for an overview of SFDR reporting requirements.

ESG data collection and reporting challenges explored

A lack of availability (or at least lack of easy access) and low quality of the varied data and information sets under consideration are the two biggest challenges to implementing effective ESG strategies across real estate portfolios. Let's take one example of a data-point at each of the three levels relevant to an investment fund manager and look at the typical journeys involved with gathering this data to bring the challenges to life:

Corporate-level

Example:
Fulfilling the GRESB request for a documented policy or procedure applicable across the funds; and providing evidence of that procedure being effectively implemented.

Best case scenario:
The development and deployment of a clear written procedure around pre-acquisition will facilitate the creation of multi-page reports detailing assessments against multiple environmental and social performance criteria and the impact of those assessments on the final investment decisions. Such criteria will likely include physical climate risk, carbon footprint and performance on indoor environmental quality metrics.

Challenges in practice:
This should be a fairly straightforward task, should the procedure and process for providing the evidence exist. If not, then a lengthy process of creating and implementing the procedure needs to begin.

Portfolio level

Example:
Reporting on the percentage split of Energy Performance Certificate (EPC) ratings for the whole portfolio, and for both investors and regulators, the carbon footprint for the portfolio, perhaps split by asset-type or region for greater granularity.

Best case scenario:
To collect either of these data-sets in a best-case scenario would mean making a request of your sustainability manager, or being in a position to download that information directly from a property database which stores the information on an asset by asset basis.

Challenges in practice:
Multiple stakeholders may hold this information, and in different places. In the case of creating an EPC data-set, the information holders might be legal teams, the asset managers, the fund manager in charge of the original deals or the property managers. This, coupled with the need to then transpose the pertinent information into one documented system before being able to process the calculation, can make for an extremely time-consuming and onerous process.

Building or asset-level

Example:
Collecting quarterly or annual electricity consumption data backed up by invoice evidence.

Best case scenario:
A dedicated building manager carefully tracks the energy spend for service charge purposes on a regular basis (as is often the case with a landlord-controlled prime multi-let office asset). The data is automatically transferred from half-hourly meters to an energy bureau and, from there, directly into the sustainability database.

Typical challenges encountered:
Tenant-controlled assets can be problematic. There is usually no particular legal or business reason for the tenant to provide that data. Even if the tenant does willingly collate and provide the consumption data, rarely would they also provide the invoice evidence required to assure the data. The data quality can also be affected if there have been manual errors in the collation that can't be picked up through a verification process.

Overcoming the challenges

Allocate resources to collecting only data that's critical to achieving your objectives.

The 5 golden rules

1. Focus only on what is material. Allocate resources to collecting only data that's critical to achieving your objectives – whether that be to comply with legislation, to add value, to reduce risk or to enhance reputation.

2. Embed data collection at corporate, fund and asset-level. At asset-level, this likely means you will need to create a data collection process for each stage of the asset-lifecycle, from pre-acquisition through refurbishment, to operating the building/engaging with your tenants, and finally to sale.

3. Engage and train your internal stakeholders and third parties (especially building managers) on the precise metrics to collect data against, and the systems to use, so that all those involved in data collection understand the bigger picture and why having reliable data is so important. Initial training sessions and simple engaging guides will ensure increased future engagement.

4. Invest in helpful technology and reporting systems, e.g., smart metering and automatic data collection systems, wifi-enabled building-sensors, user-friendly online databases, hand-held data reporting devices and smart BI reporting processes.

5. Invest in the talent and tools to draw real insights out of your data, ideally using cutting edge data science methods to highlight the key risks and opportunities across both your organisation and your portfolio, so that you can take appropriate action.

The path to best practice

Fund managers excelling in ESG collection and reporting, typically do the following:

Data analytics is no longer just for data scientists and experts.

1 Embrace automation

As the potential amount of the environmental and social data that can be collected increases, particularly at building level, automation becomes a necessity rather than a nice to have. Sensors, automatic meters and API connections can now send data directly to analytical databases, which, among other benefits, notably, removes human error and also significantly cuts down on labour costs.

IoT (Internet of Things) devices are becoming more popular within the sustainable property space for automatically collecting and transmitting data on various aspects of building performance and quality of life metrics such as energy consumption hotspots, indoor CO_2 concentrations, noise levels and air temperatures, local air pollution statistics, and even biodiversity metrics on green roofs.

2 Adopt a data-driven culture and mindset

Data analytics is no longer just for data scientists and experts. Now everyone from a building manager to an engineer, or a construction site manager to a corporate office tenant can analyse their own data and gain vital information using increasingly capable and easy to operate business intelligence platforms.

3 Invest in the user experience

Users want their analytics tools to be simple and engaging and business intelligence platforms are giving them the user-friendly, no-coding alternatives they need. For example, Tableau software now allows users to view their data analytics on the go with smart phone apps. In the real estate sector that means that the building manager can see the impact on the energy consumption of the practical changes they are making in the building in real time. No longer do you require a deep knowledge of statistical mathematics to perform data analytics processes such as regression analysis.

4 Drive efficiency through platform integration

Over the last five years there has been an explosion of new SAAS ESG automation platforms such as Deepki and Measurabl that include everything an end user needs within one platform, obviating the need for several different tools. These platforms include automation of the collection of utility data, automatic issuance of surveys to collect qualitative asset-level information - such as EPC ratings, building certifications and the nature of technical efficiency measures installed on site - business intelligence layers, regression analysis of degree days and many more functions to help any ESG manager understand the impact of the data they hold.

5 Make data analytics a core business function

For any organisation, data analytics is becoming a core function and this is even more true in the ESG space. The core of any successful ESG strategy is good data management – if you are spending large amounts of money based on what the data is showing, for example taking decisions to upgrade multiple HVAC systems in buildings, or training sections of your workforce on unconscious bias, it is paramount that the data is correct and you're seeing the whole picture.

An eye on the future

Emerging trends shaping the future of ESG data collection and reporting:

The digital transformation of real estate - 'what gets measured gets managed'

This sees innovation arising in every aspect of the industry, offering solutions on how the property sector should respond to the major trends of e-tail, health and wellbeing focus, co-working/co-living, the shift to the low carbon and circular economy, and even successfully adapting to climate change.

Live reliable data is fundamental to grabbing and utilising all the opportunities that this new environment has to offer. At asset-level, it provides a better understanding of what is happening inside and around buildings, what initiatives are successful, and which are not, based on quantitative analysis (which also helps override outdated perceptions). It improves reporting and allows bottom-up decision making.

Real time understanding of ESG performance reveals areas of higher risks and opportunities for investments, and live data helps building managers to avert problems; for example, power blackouts due to a sudden ramp-up of air-conditioning in the local area during a heat-wave, or early warning alerts for surface water flooding due to a downpour.

Legislation moving towards mandatory key performance indicators

The EU SFDR regulations have now mandated disclosures for investment managers on integration of sustainability risks into the investment decision-making process and on 'principle adverse sustainability impacts' using defined KPIs. The EU Taxonomy requires mandatory disclosures aligned with six impact areas. In the UK, the Government is also committed to developing its own Taxonomy.

Harmonisation of voluntary reporting frameworks

While the plethora of available sustainability and ESG standards for businesses has supported the improvement of corporate sustainability performance and reporting, in parallel it has caused a level of confusion in selecting the relevant standards. In turn, organisations are increasingly seeing the need for consistency and collaborating in the creation of aligned global reporting frameworks. For example, CDP and GRESB have both aligned their climate risk reporting requirements to the disclosure recommendations of TCFD.

Requirement for transparency from investors

AREF and the Aztec Group's recent research report, "Real estate fund operations of tomorrow", ranked 'increasing importance of ESG issues' and 'greater demands for transparency from investors' as the first and second most important trends in European real estate driving structural change over the next three years. The survey participants also ranked 'increasingly strict ESG disclosure rules' as the second greatest challenge currently facing the real estate industry in Europe. Those points both speak to the same desire from legislators and voluntary reporting initiatives to streamline and specify the ESG indicators reported on, in order to provide greater clarity on investor performance and real-world outcomes.

Final thoughts…

In conclusion, reliable data is a tool for real estate investment managers to increase their buildings' contribution to social and environmental value as well as financial value, protecting them from obsolescence in the long-term.

If an investment manager can demonstrate access to robust, even live, data across all the material KPIs for their organisation and portfolio and generate insightful analysis on the back of it to feed into their investment decision-making, the plethora of disclosure initiatives may well fall away as the real world outcomes will be able to speak for themselves. Data, ultimately, is the key to creating a sustainable future for the built environment and beyond.

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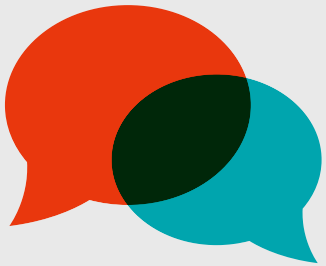

Appendix 1

Source: TCFD, Recommendations of the Task Force on Climate-related Financial Disclosures, 2017. Original source linked here

Recommendations and supporting recommended disclosures

Governance

Disclose the organisation's governance around climate-related risks and opportunities.

Recommended disclosures

a. Describe the board's oversight of climate-related risks and opportunities.

b. Describe management's role in assessing and managing climate-related risks and opportunities.

Strategy

Disclose the actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy, and financial planning where such information is material.

Recommended disclosures

a. Describe the climate-related risks and opportunities the organisation has identified over the short, medium and long term.

b. Describe the impact of climate-related risks and opportunities on the organisation's business, strategy, and financial planning.

c. Describe the resilience of the organisation's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.

Risk management

Disclose how the organisation identifies, assesses, and manages climate-related risks.

Recommended disclosures

a. Describe the organisation's processes for identifying and assessing climate-related risks.

b. Describe the organisation's processes for managing climate-related risks.

c. Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management.

Metrics and targets

Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.

Recommended disclosures

a. Disclose the metrics used by the organisation to assess climate-related risks and opportunities in line with it's strategy and risk management process.

b. Disclose Scope 1, Scope 2 and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.

c. Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets.

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Appendix 2

JLL overview of SFDR periodic reporting requirements for a real estate fund designated as 'Article 9'. Original EU source linked here

To what extent was the sustainable investment objective of this financial product met?	What were the top investments of this financial product?	What was the proportion of sustainability related investments?	What actions have been taken to meet the sustainable investment objective during the reference period?	How did this financial product perform compared to the designated reference benchmark?	How was the objective of a reduction in carbon emissions aligned with the Paris Agreement?
Publish performance against sustainability indicators, for the current reporting period and previous periods (i.e., historical comparison)	List of investments constituting the greatest proportion of investments of the financial product during the reference period	Template provides a diagram to show asset allocation Disclose purpose of investments which are "other", whether any E or S safeguards were applied to these investments Disclose how principle adverse impacts were considered; alignment with OECD GMEs and UN GPs on Business &Human Rights Disclose the economic sectors in which the investments were made	No mandated structure to this segment	To include where an index has been designated as a reference benchmark for attainment of the sustainable investment objective Explain how the reference benchmark differs from a broad market index Disclose how the product performed against sustainability indicators Disclose how the product performed compared with the reference benchmark Disclose how the product performed compared with the broad market index	Include a description of the contribution of the financial product during the reference period to achieving the objectives of the Paris Agreement, including in respect of an EU Climate Transition Benchmark or EU Paris-aligned Benchmark, the ESG factors and criteria considered by the benchmark administrator in accordance with Commission Delegated Regulation (EU) 2020/1818.

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About the Aztec Group

Established in 2001, the Aztec Group is an award-winning independent provider of fund, corporate and depositary services, employing over 1,300 people across Guernsey, Jersey, Luxembourg, the UK and the US.

Owner-managed, the Group specialises in alternative investments, administering more than €440 billion in assets, 450 funds and 4,500 entities for a range of clients spanning the major asset classes, including real estate, private equity, venture capital, private debt and infrastructure.

Supporting over 240 alternative investment managers, the Group prides itself on its long-term partnership approach, enhancing clients' fund operations through industry-leading expertise, technology and controls, with a dedicated relationship team by their side over the life of their funds.

For further information, visit **aztecgroup.co.uk**

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About JLL

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