Building on the future

■ By **René Didde** ■ Photography **ANP, Getty Images**

For the past 20 years sustainability has usually been associated with industries accused of polluting or depleting our environment, such as manufacturing and transport. Today, the long-term benefits that sustainability can bring also apply to the real estate industry.

Underlining the increasing importance of sustainability, the umbrella organisation ICSC (International Council Shopping Centers) announced this summer that it would grant an annual sustainability award for European shopping centres. The finalists will be announced in November and the winner will receive the award at the ICSC's annual conference in Warsaw in late April 2007. This new accolade is indicative of the trend of increased international focus on sustainability in the real estate industry. 'Sustainability' has been a fashionable buzzword since the mid-1980s: it describes economic developments that have no detrimental repercussions for people or the environment. The so-called '3 Ps' are a succinct and useful guideline: Profit, People, and Planet.

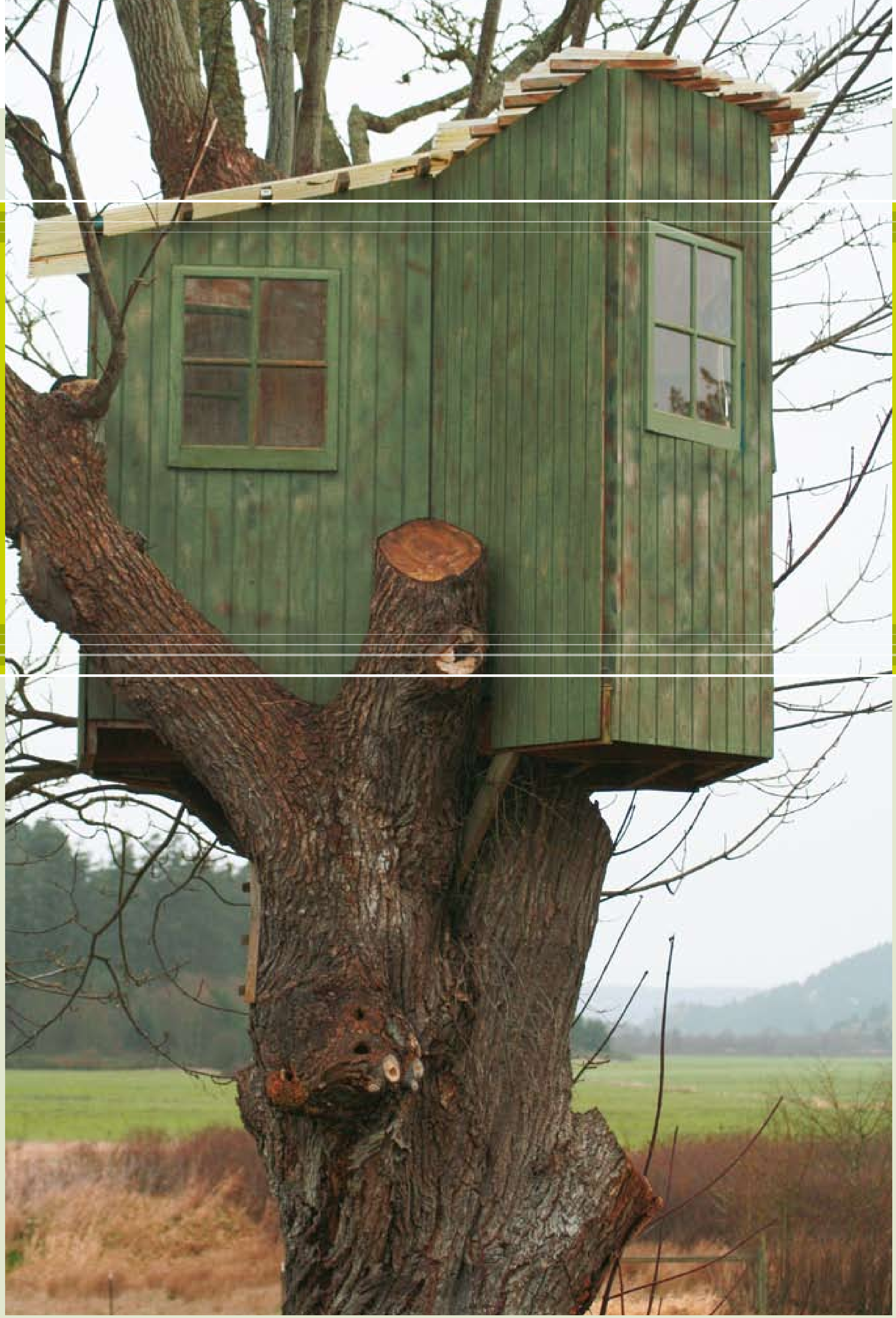
Now, 20 years later, many companies take pride in their sustainability policies: they are sensitive to the environmental impact of their production process, they monitor their energy use and try to reduce their consumption of natural resources. And ever since environmental action groups first attracted media attention by highlighting the depletion of the rainforests, banks too are more aware of the impact their financing activities have on the environment. More and more companies are demonstrating their accountability by presenting shareholders and stakeholders with sustainability reports, checked by accredited auditors in the same way as the more traditional variety of annual reports.

Environmental requirements

The publication of sustainability reports has not yet become standard practice in the real estate industry. "But sustainability is more of an issue than it used to be," says Dimitry Melchiors, Director of Special Projects at Bouwfonds Property Finance. "Particularly as the Dutch building code stipulates a number of environmental requirements for buildings." The building code he alludes to is important because if it's not adhered to it's impossible to obtain a building permit, which is like a sacred document for real estate financiers.

One such environmental requirement laid down in the building code is the energy performance standard, which is comparable to an energy consumption yardstick that a building must comply with. In any building the values of things like the insulation coefficient of the walls, roof and windows, the heating and hot water systems and the air-conditioning, are compared to exact parameters. The government regularly tightens these requirements, contributing to a process that is improving the energy efficiency of a whole new generation of buildings. "As financiers, we have no direct involvement in specifics like these," says Melchiors, who, together with the Special Projects department at Bouwfonds, is closely involved in financing complex and long-term inner-city restructuring projects. What these projects have in common is mixed use, a balanced blend of living, working, parking, leisure, public space and greenery – in other words, key concepts that each have some bearing on long-term sustainability. Early on in the process, however, it's developers, rather than financiers, who make specific demands. "Developers can decide on the type of outer walls, for example, or whether to incorporate innovative features like underground thermal storage systems."

Given the current (and, presumably, continuing) high cost of energy, a building's energy performance is becoming



increasingly important for potential owners or tenants. "Advertisers haven't yet reached the stage where they include a property's energy performance in advertisements," says Melchiors. "However, in addition to traditional criteria like look and feel, parking facilities and layout, energy performance is increasingly becoming a determining factor for a building." Other sustainable construction factors include using a minimum of materials, using recycled materials (like recycled concrete aggregate in the foundations), and timber sourced from sustainably managed forests.

A building's marketability is key, insists Melchiors: "Sustainable construction must be affordable." Arjen van Rijn, Director of Bouwfonds Property Finance International, agrees. He concedes that while a developer always has the most profit potential from a building that costs less to construct, the trend is shifting towards differentiation. "The focus is moving towards responsible entrepreneurship," he confides.

Setting the tone

Van Rijn believes that in addition to using sustainable materials and using energy efficiently, a good location and an optimum user environment are also key factors. There is a growing awareness, both in the Netherlands and elsewhere in Europe, that businesses are perfectly capable of reconciling sustainability and cost reduction. Citing Sir Norman Foster's Swiss Re – locally dubbed as the Gherkin – in London City as a good example, Van Rijn explains that the aerodynamic, glazed shape of this highly acclaimed design optimises sunlight and ventilation and is extremely energy efficient. Another example is the Sonae Sierra shopping centre in Brazil, where 100 per cent of the concrete is sourced from demolition material. "Examples like these are setting the tone in the real estate industry," he asserts.

It is Bouwfonds' contention that using energy and materials wisely in certain parts of a building gives users an immediate financial advantage and that sustainable buildings can generate cost savings across the board. "Giving buildings a flexible layout extends their economic lifespan, potentially increasing returns for investors," says Van Rijn. "What's more, with oil prices being what they are, marginally higher investments in sustainable systems can be recouped quickly."

Sustainable real estate also lends itself to long-term projects. Indeed this is a trend that's already well established in public-private partnerships. "In so-called Design Build Finance Maintain Operate agreements, contracts are closed for a period of 25 years, which also includes financing the operational costs," says Van Rijn. "The challenge facing private stakeholders is to find a balance between acceptable all-in construction costs and low operational costs. It usually results in energy-efficient and low-maintenance solutions, which improve sustainability."

Quality

Sustainability is gaining ground in the financing of real estate, but it is already well established in development. "A house with a grass roof might seem quite advanced in that it's very efficient at retaining heat, but it's still a niche market, and one that leaves many consumers cold," asserts Bas van de Griendt, environmental manager at Bouwfonds MAB Development. He applauds the fact that the term 'quality' nowadays also includes and guarantees sustainability criteria. "A certain level of quality must be attained when dealing with what the Greeks saw as the four natural elements of earth, water, air and fire – or energy. Our houses have this quality."

According to Van de Griendt, sustainability and the 3 Ps are no longer just corporate rhetoric mouthed by PR departments. "Those days are over. I'd prefer a project with modestly concealed systems to one with prominently visible solar panels. These might look environmentally friendly, but the energy savings they generate are negligible." The quality of construction materials must also meet sustainability criteria. Timber from sustainably managed forests is durable and requires little maintenance," he says, estimating that 10 per cent of the door and window frames installed in Bouwfonds homes are manufactured from FSC (Forest Stewardship Council) timber. "This is one way in which we acknowledge our responsibility for the social context in which we operate."

Van de Griendt observes that the environmental awareness of private homeowners is often less than that of office developers and housing corporations, mainly because of the more calculated approach taken by the professionals. "Consumers prefer to have five square metres more living area than lower energy bills." This is one of the reasons, he explains, that many more offices than private homes are equipped with thermal storage systems – sophisticated energy systems that exploit the heat and cold retention qualities of water stored deep underground. During the summer, they pump up relatively cool water for air-conditioning, while in the winter they supply warm water for heating. Van de Griendt: "After a really hot summer like the one we've just had in the Netherlands, an investment in such a system will look more attractive to consumers."

Swiss Re (far left) and the offices of the Triodos Bank (left) illustrate that design and sustainability are highly compatible. Timber from sustainably managed forests (above) is durable and requires little maintenance.

> "Businesses are perfectly capable of reconciling sustainability and cost reduction"

Roelof Balk, Director of Bouwfonds Fund Management, thinks that sustainability in real estate is not confined to bricks, mortar and soil, but, increasingly to the total area development. "In addition to the natural environment, industrial heritage is now also more important in real estate activities," he observes. For example, disused factory complexes listed as being of historical importance can be renovated and given a contemporary look and purpose. "By studying the surrounding environment and adapting the look and feel of new construction to blend in with the character of existing buildings, you create a new dynamism," says Balk.

According to Balk, the increasing focus on sustainability also extends to real estate funds. An example is Bouwfonds Asset Management's involvement in the Triodos Sustainable Real Estate Fund. This was established in 2004 and with an asset base of €25 million, it invests in sustainably built or renovated business premises and listed sites. The long-term returns are estimated at six per cent (excluding the real estate's increase in value.)

Tax incentives

So sustainability does indeed yield returns and add value. "Existing operational models for new construction can be adapted and combined with those for natural areas," says Balk. "In this way we have calculated that the revenue from one hectare of new construction in a green belt area can pay for the conservation of ten hectares of new green area." The long-term returns are satisfactory, as these green areas – often near water – are attractive to potential buyers and can be marketed as part of tourism or even healthcare-related projects." The Dutch government helps by providing tax incentives to get such environmentally friendly projects off the ground. Investors put cash into a green fund, and agree to accept a slightly lower interest rate than usual in exchange for a 2.5 per cent tax break from the government. Financiers of environmental projects that have been approved to do so can borrow money at a lower interest rate. With interest rates gradually rising, these funds are becoming more important. To the best of Balk's knowledge there are no similar fiscal initiatives anywhere outside the Netherlands, but he concedes that other European countries are exploring the possibilities. "However, given the various tax regimes in Europe, this Dutch initiative will probably not be an easy one to follow."