Principles for Responsible Investment

# RESPONSIBLE INVESTMENT TRENDS IN REAL ESTATE

## INSIGHTS FROM PRI REPORTING DATA

**SEPTEMBER 2024**

An investor initiative in partnership with UNEP Finance Initiative and UN Global Compact

# THE SIX PRINCIPLES

## PREAMBLE TO THE PRINCIPLES

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

1 We will incorporate ESG issues into investment analysis and decision-making processes.

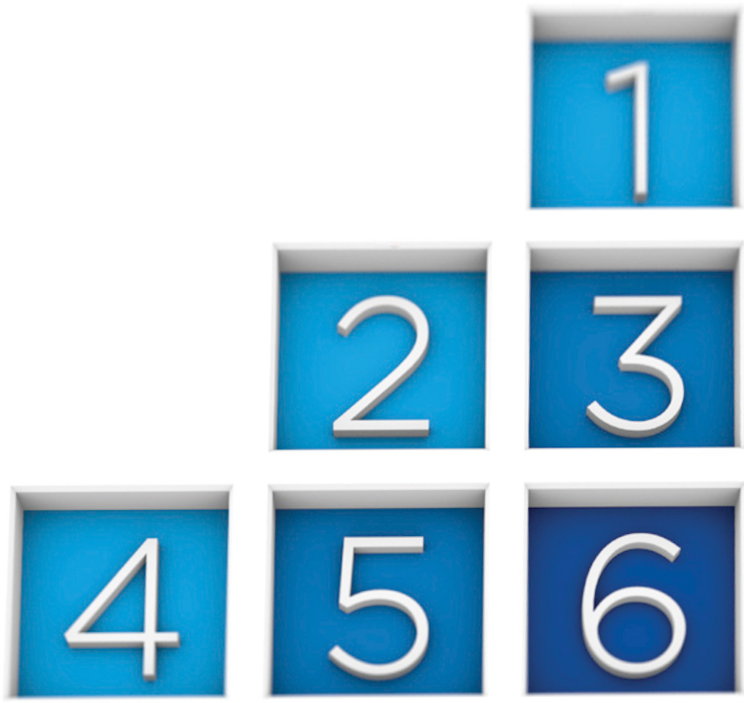
2 We will be active owners and incorporate ESG issues into our ownership policies and practices.

3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.

4 We will promote acceptance and implementation of the Principles within the investment industry.

5 We will work together to enhance our effectiveness in implementing the Principles.

6 We will each report on our activities and progress towards implementing the Principles.




## PRI's MISSION

We believe that an economically efficient, sustainable global financial system is a necessity for long-term value creation. Such a system will reward long-term, responsible investment and benefit the environment and society as a whole.

The PRI will work to achieve this sustainable global financial system by encouraging adoption of the Principles and collaboration on their implementation; by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.

# EXECUTIVE SUMMARY

This report analyses data from the 2023 PRI Reporting Framework, focusing exclusively on insights from the policy, governance and strategy (PGS) and real estate (RE) modules. The findings indicate advanced responsible investment practices by real estate investors, as well as areas where further progress can be made.

Real estate investors are increasingly integrating human rights considerations and climate-related metrics into their investment strategies, reflecting an understanding of the direct impacts these factors can have on investments, and vice versa. However, some gaps remain, particularly on human rights, where the comprehensive use of frameworks such as the UN Guiding Principles on Business and Human Rights, a foundational baseline for investors to take action on human rights, appears limited.

The data suggests that while the vast majority of real estate investors are increasingly integrating asset class specific ESG guidelines into their responsible investment policies, far fewer incorporate responsible investment commitments into constitutive fund documentation. This dichotomy suggests a foundational understanding and acceptance of ESG principles across the sector, but less willingness or capacity to enshrine the same into formal commitments and action.

Green building certifications are most commonly used to inform ESG materiality analysis in real estate, reflecting a consistent approach within the industry. However, this can result in a greater focus on environmental as opposed to social or governance factors given that certifications tend to cover the former in more detail. While it is common for real estate investors to use green building certifications when analysing potential investments, nonetheless most signatories report that only a minority of their assets actually receive the certifications. This is possibly due to the resources required and the limited focus on ongoing operational performance.

Post-investment, the data indicates that real estate investors understand the importance of strong ESG risk management and value creation practices. However, implementation appears inconsistent, particularly among smaller investors who may lack the necessary resources for consistent action.

Similarly, at exit, the data points to how strong ESG practices and performance may influence the attractiveness of assets to potential buyers, with larger investors particularly proactive in sharing ESG-related information.

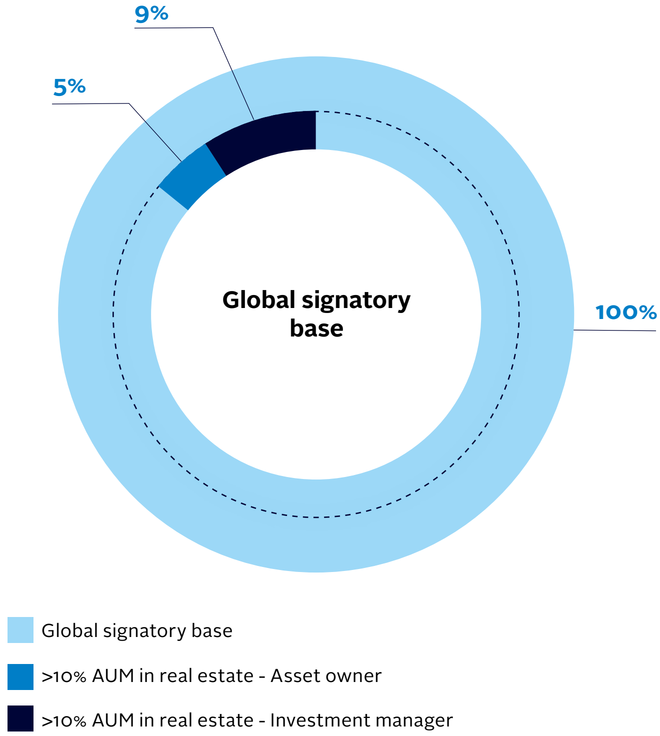
# ABOUT THE DATA

## POLICY, GOVERNANCE AND STRATEGY MODULE:

- The data analysed in this module was publicly disclosed by signatories during the 2021 and 2023 reporting cycles.
- The data covers signatories with >10% AUM in real estate, or 395 signatories.
- The data was highly correlated, yet it is important to note that this does not necessarily confirm causation, given the sample of investors have holdings across asset classes.
- There have been some changes in indicator wording from 2021 to 2023. Only data points considered equivalent across both reporting cycles have been analysed.

## REAL ESTATE MODULE:

- The data analysed for this module was publicly disclosed by signatories during the 2023 reporting cycle.
- The data cover signatories with >10% AUM in real estate, or 244 signatories.
- Where some questions are not applicable to the full sample, percentages have been calculated using as denominator the number of signatories for which the indicator is relevant / applicable.
- Asset owners did not report on asset class modules in 2023, meaning that the analysis covers only data from investment managers.

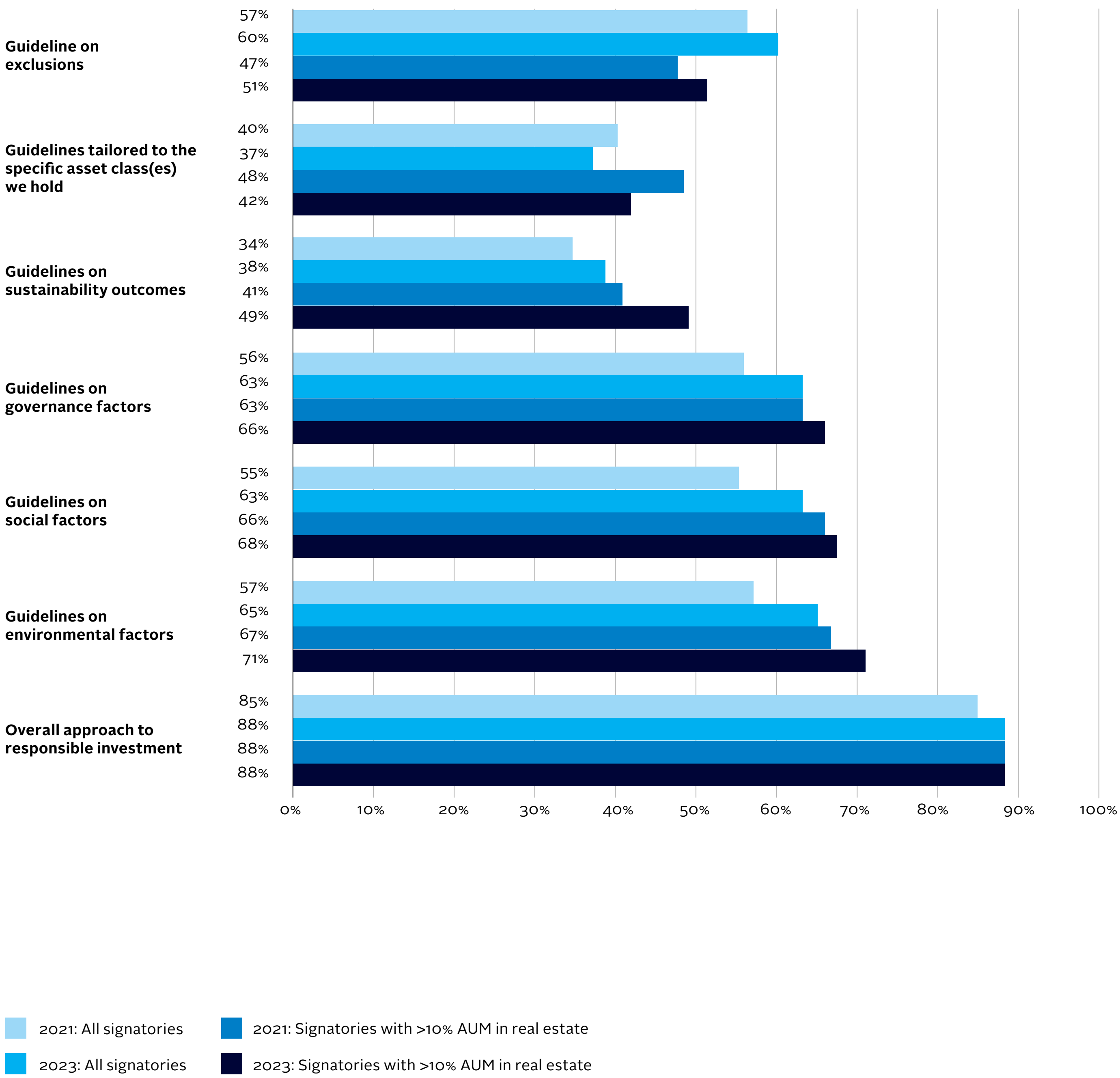


# RESPONSIBLE INVESTMENT POLICY ELEMENTS MORE LIKELY TO BE PUBLIC

Real estate investors' guidelines on ESG and outcomes are more likely to be public than for signatories as a whole. This could be attributed to:

- a long-standing focus on sustainability, notably energy efficiency, within elements of the real estate industry;
- a broad recognition of how ESG factors, such as physical climate risks, can impact real estate, and of how real estate can impact those same ESG factors (high carbon emissions, health and safety risks etc);
- demand from clients and beneficiaries for investors to take action.

**Which elements of your formal responsible investment policy(ies) are publicly available?**



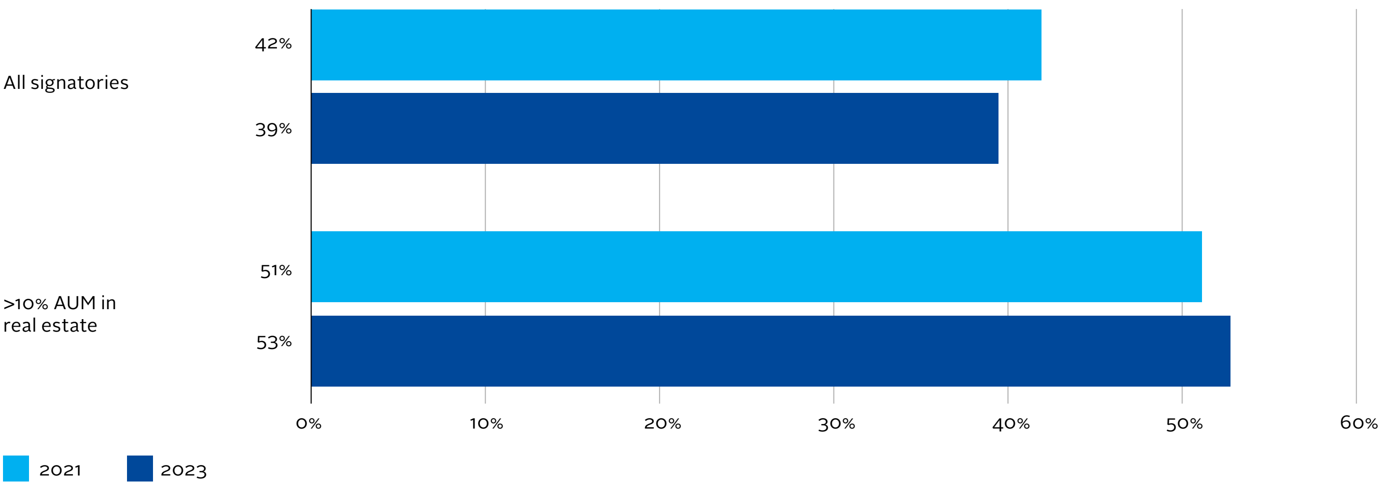

**Source**: Indicator PGS 3. Indicator denominators for 2023: 2859 (global signatory base), 395 (real estate investors).Denominators for 2021 (ISP 2): 2341 (global signatory base), 234 (real estate investors)

# REAL ESTATE INVESTORS MAKE GREATER USE OF CLIMATE SCENARIOS

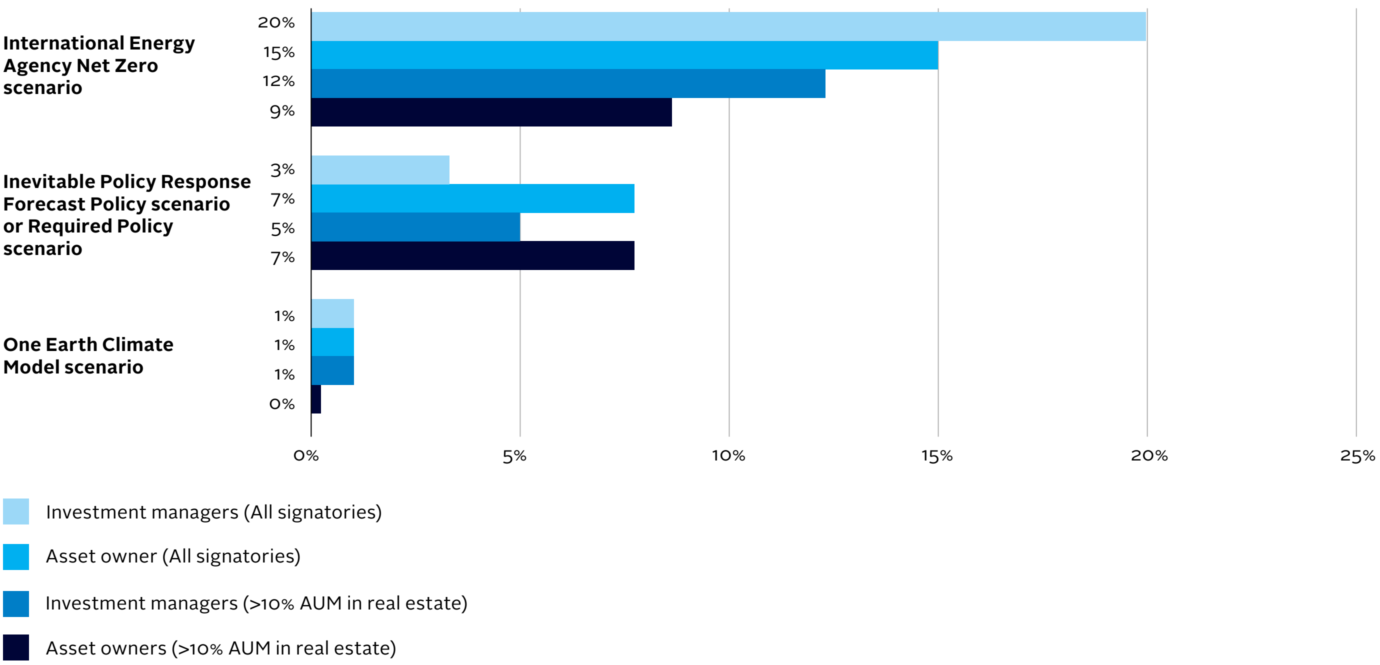
Investors in this asset class are more likely to use climate scenarios to assess the resilience of investment strategies. This can be attributed to:

- the significant impact on real estate of physical and transition climate risks, such as extreme weather and regulatory changes;
- the potential for property values and operational resilience to decline;
- increased market expectations around sustainability.

### Yes, my organisation has assessed at least one climate scenario




### Climate scenario source




**Source**: Indicator PGS 43. Denominators 2023: 2859 (global signatory base), 395 (real estate investors). Denominators for 2021 (ISP 33): 2341 (global signatory base), 234 (real estate investors)

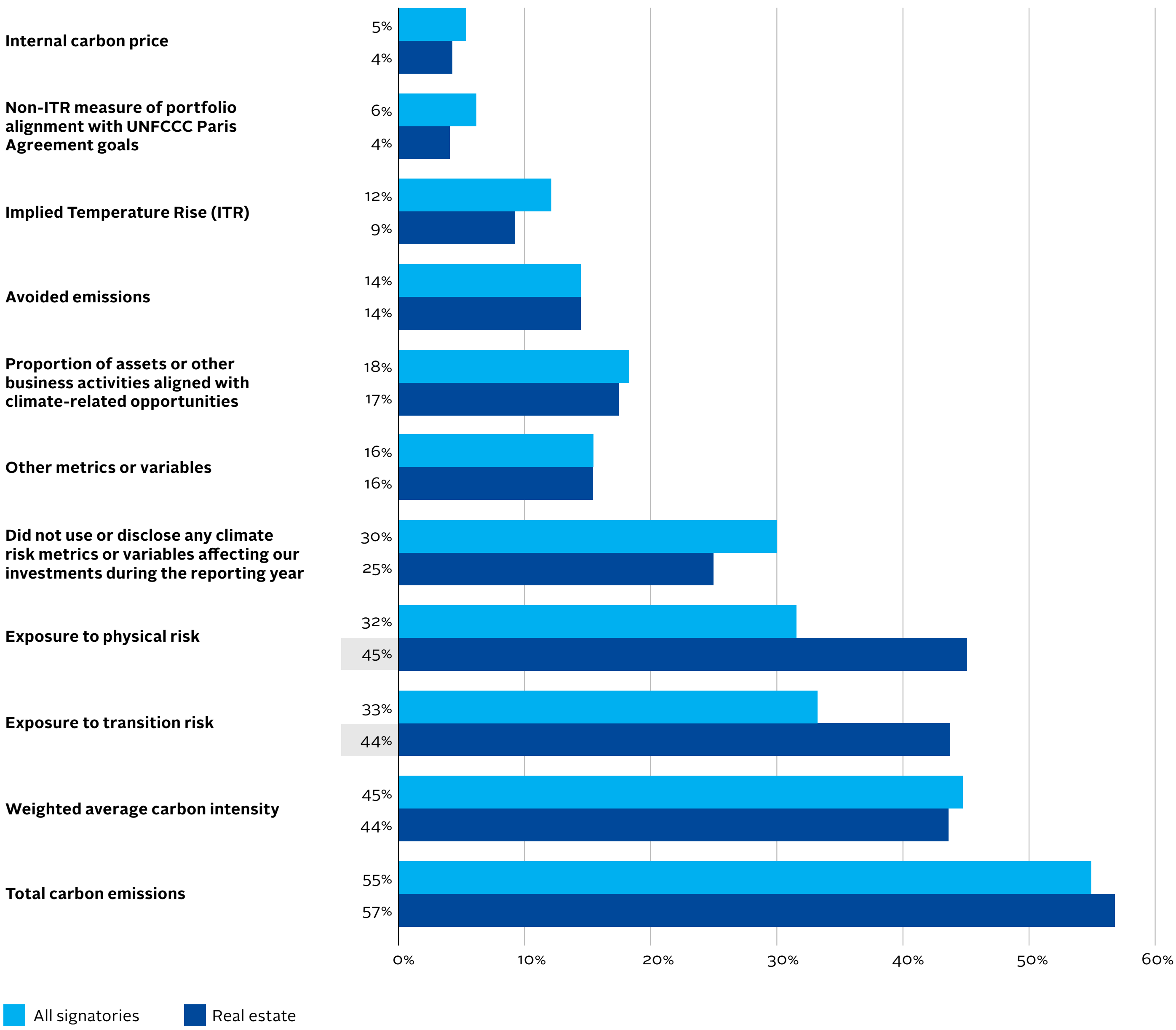
# MORE REAL ESTATE INVESTORS SHARE DATA ON TRANSITION AND PHYSICAL RISKS

The greater use of metrics related to transition and physical risks likely stems from factors such as the direct impact of such risks on real estate and the long-term timeframe of real estate investing.

Additionally, assessing transition and physical risks can be easier in real estate than some other asset classes, given the fixed nature of the underlying assets. However, the methodologies available remain imperfect and inconsistently applied.

There remains significant scope for greater use and disclosure of climate metrics by real estate investors.

**% using and/or disclosing climate metrics**

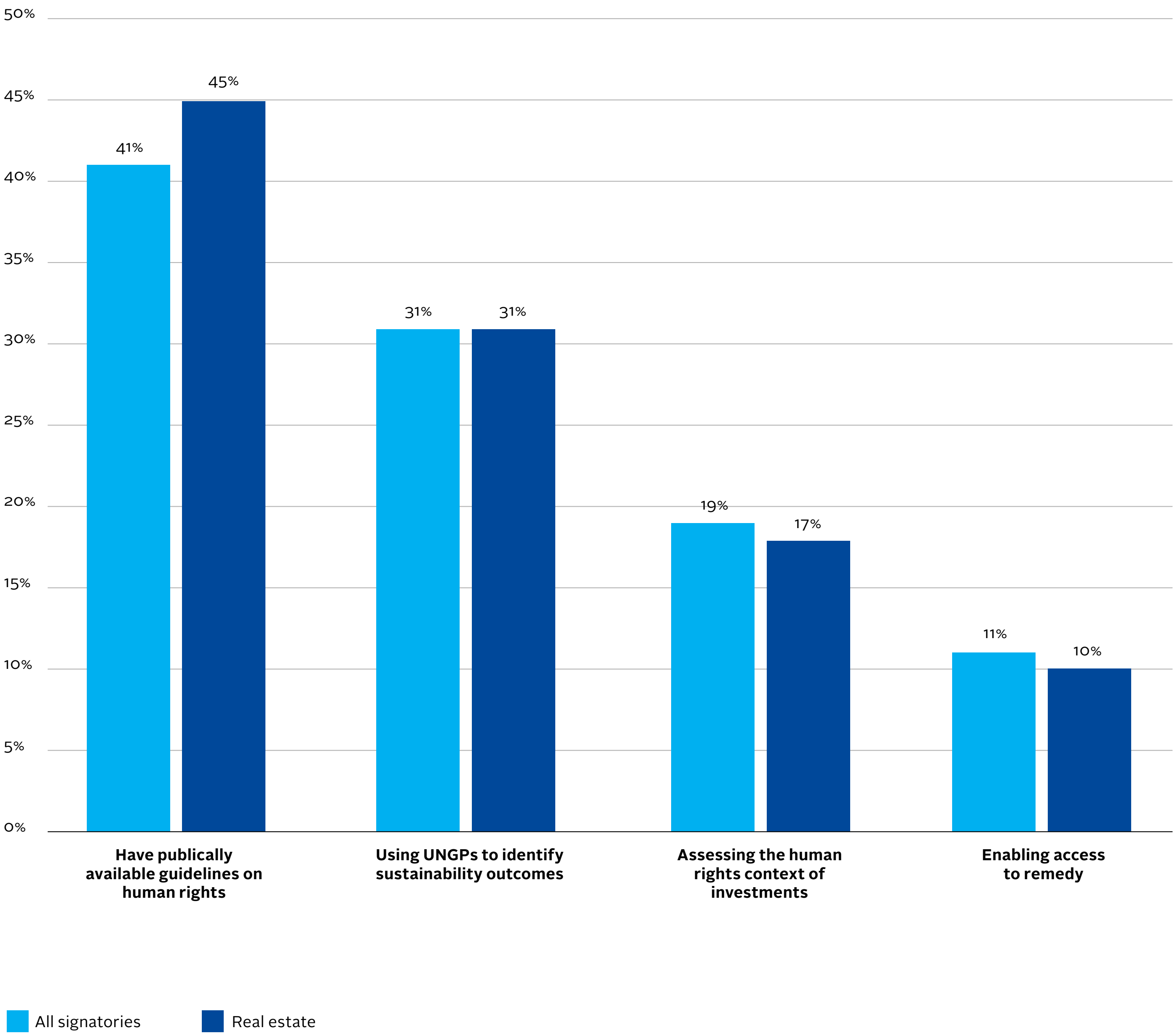



**Source**: Indicator PGS 45. Denominators: 2859 (global signatory base), 395 (real estate investors).

# UPTAKE OF HUMAN RIGHTS FRAMEWORKS LIMITED

Real estate investments have a tangible impact on communities and individuals. In many jurisdictions, there is a requirement for real estate developments to carry out social impact assessments to obtain necessary licences/permits.

- However, the figures suggest that only a third of real estate signatories fully align with the UN Guiding Principles on Business and Human Rights (UNGPs).
- A small minority enable access to remedy where appropriate.
- This underlines the need for more systematic processes to identify, assess and mitigate human rights impacts.



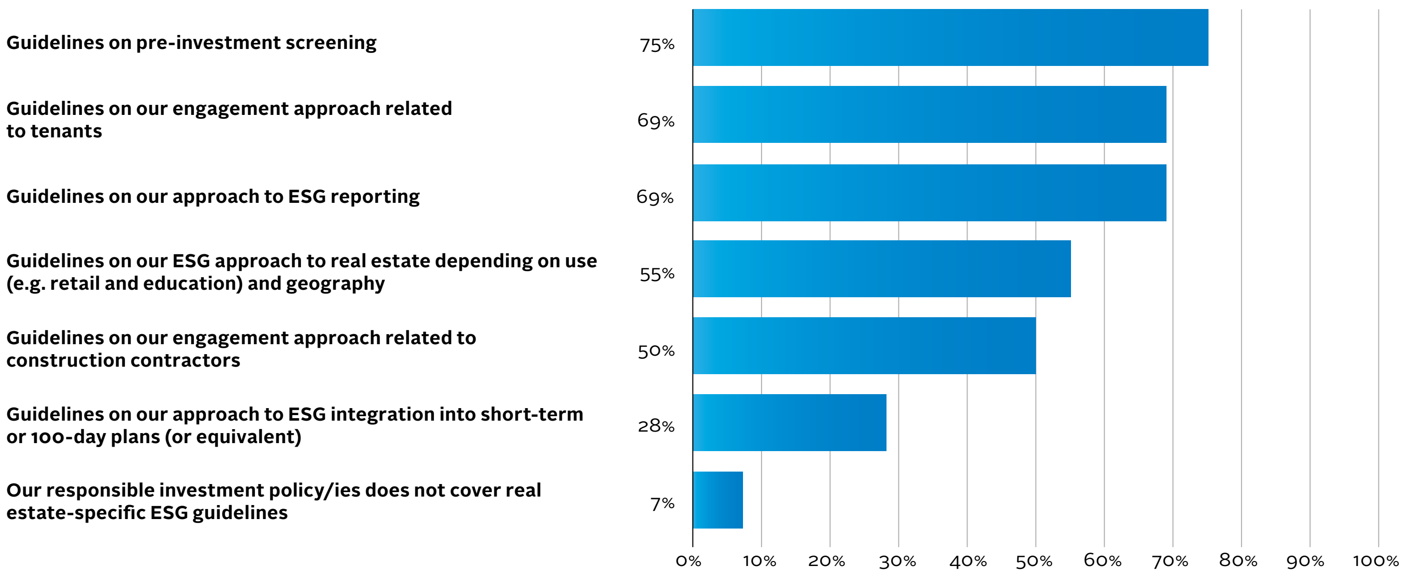

**Source**: The graph presents figures from multiple indicators: PGS 3, PGS 47.1, PGS 49, and PGS 50.
Denominators: 2859 (global signatory base), 395 (real estate investors).

# ASSET CLASS-SPECIFIC ESG GUIDELINES COMMON IN RESPONSIBLE INVESTMENT POLICIES

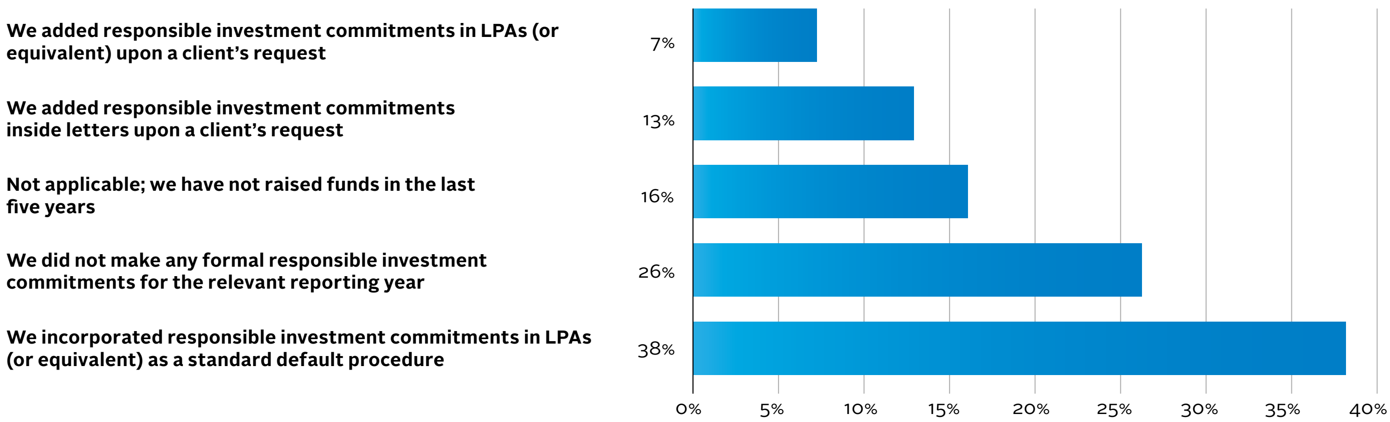
The data suggests a strong foundation for ESG integration in real estate investments across many signatories, but also points to areas for improvement. These include:

- the specificities of different real estate categories and geographic differences;
- going further into the value chain;
- integrating ESG factors post-investment;
- translating ESG guidelines into formal commitments within fund documents;
- only 38% of respondents reported routinely including responsible investment commitments in Limited Partnership Agreements (LPAs) or similar documents;
- as many as 26% did not formalise such commitments within the past year.

**What real estate–specific ESG guidelines are currently covered in your organisation's responsible investment policy(ies)?**




**For all of the funds that you closed during the reporting year, what type of formal responsible investment commitments did you make in LPAs, side letters, or other constitutive fund documents?**

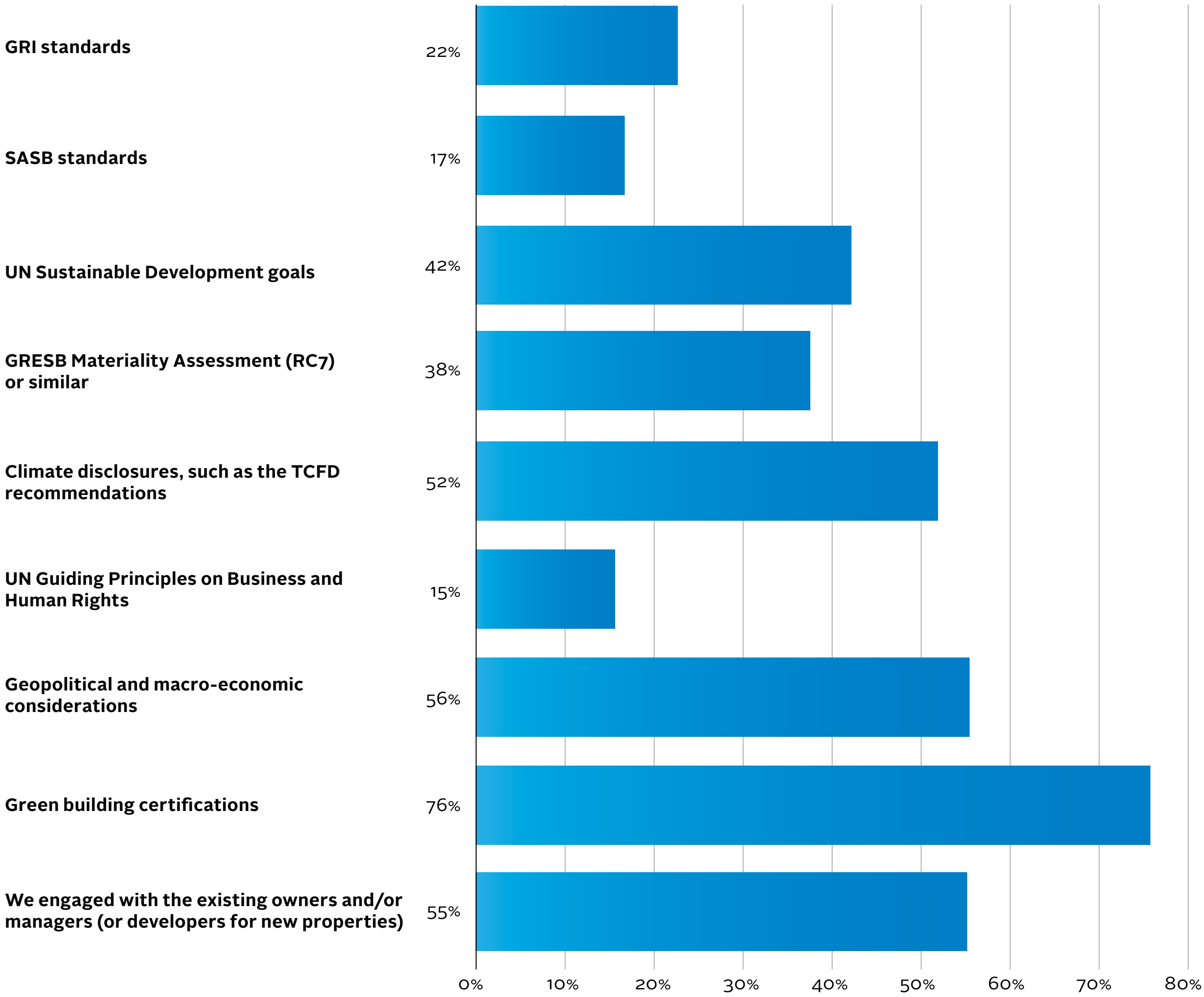



**Source**: Indicator RE 1 and RE 2. Denominator: 244 (real estate investors with >10% AUM in real estate)

# GREEN BUILDING CERTIFICATIONS POPULAR IN ESG MATERIALITY ANALYSIS

- The widespread use of green building certifications in ESG materiality analysis underscores their importance to investors, however such certificates tend to focus more on environmental factors and energy use.
- Despite their use in ESG materiality analysis, however, most signatories report that only a minority of their assets actually receive green building certifications.
- This may reflect the resources required for the certifications and/or of the fact that many certifications do not cover operational performance, limiting their value in ongoing ESG monitoring and disclosures.

**During the reporting year, what tools, standards and data did you use in your ESG materiality analysis of potential real estate investments?**

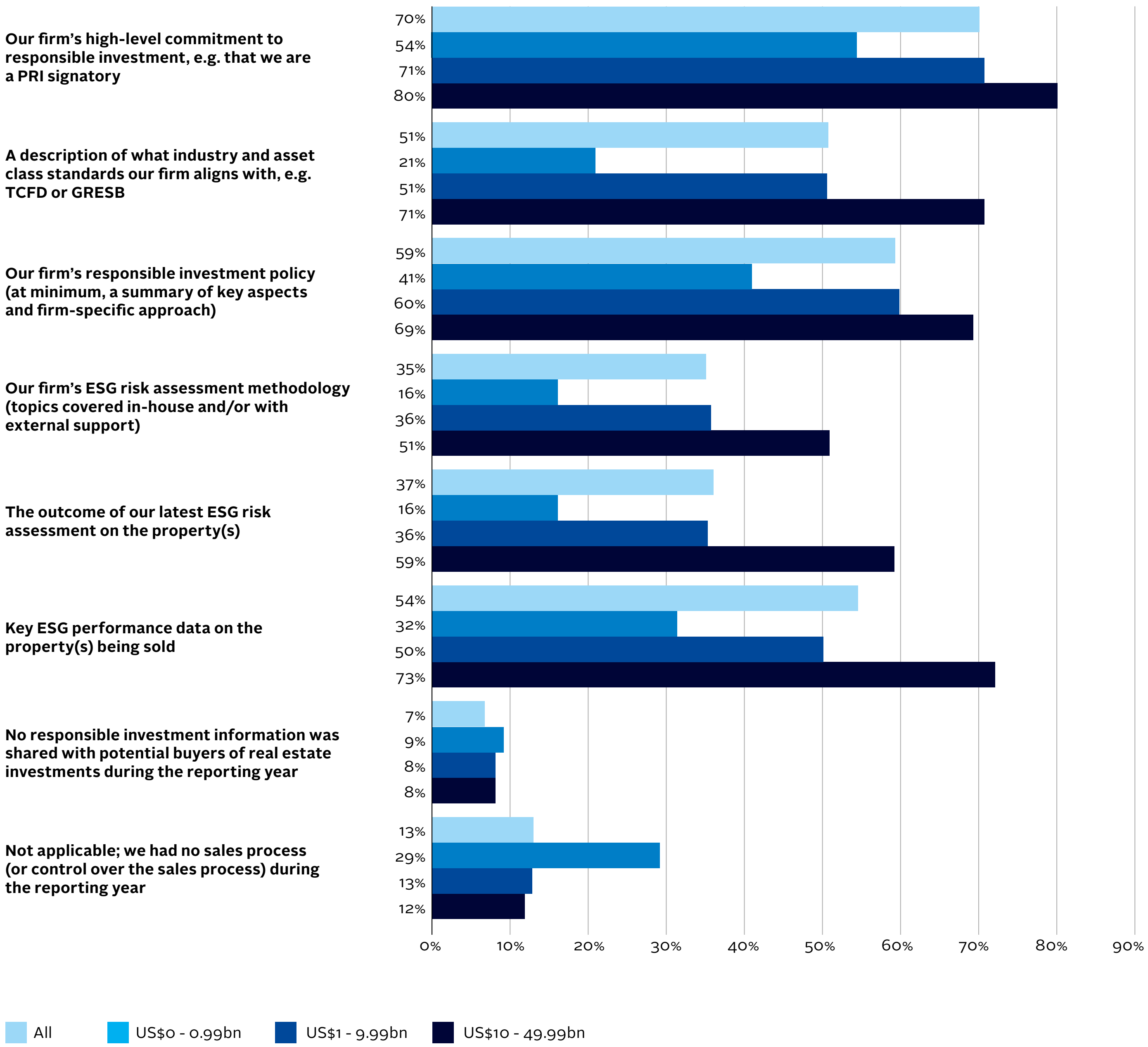



**Source**: Indicator RE 3.1. Denominator: 223 (real estate investors with >10% AUM in real estate).

# TRANSPARENCY IN ESG PRACTICES VALUED BY REAL ESTATE INVESTORS

- A significant 70% of respondents conveyed their overarching commitment to responsible investment to potential buyers.
- More than 50% shared key ESG performance data on the properties being sold and details on responsible investment policies and standards.
- This points to how ESG practices, are at the very least, a significant consideration in the value and attractiveness of real estate assets.
- Signatories with over US$10bn in AUM typically shared more information than smaller signatories, likely a reflection of greater resources.

**During the reporting year, what responsible investment information was shared with potential buyers of real estate investments?**

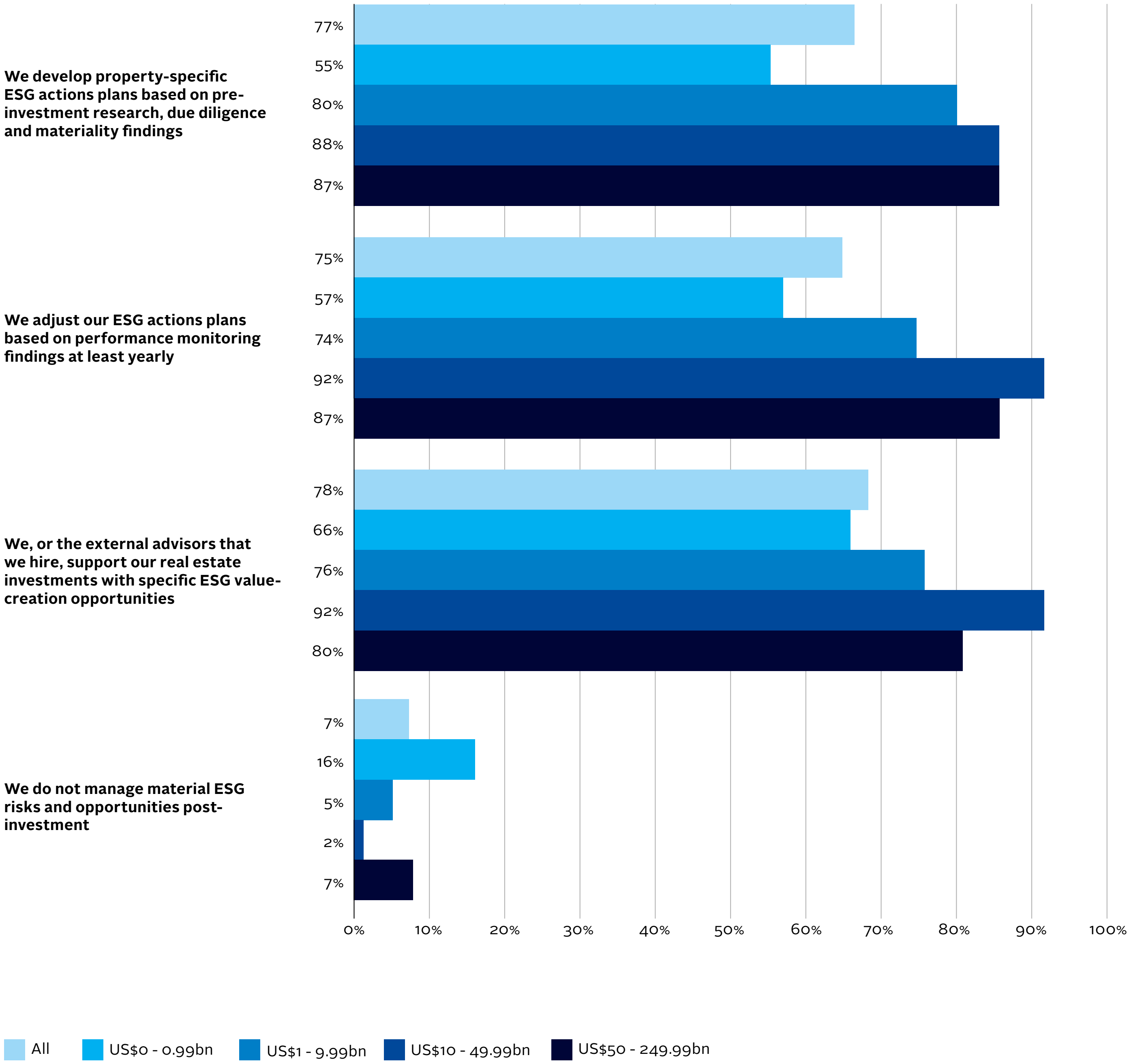



**Source**: Indicator RE 20. Denominator: 244 (real estate investors with >10% AUM in real estate). The two largest AUM bands (US$49.99-250 and 250+) are excluded due to the sample size being too small to provide meaningful insights. Percentages reflect total AUM, not AUM solely in real estate.

# INVESTORS FAVOUR ESG VALUE CREATION EFFORTS DURING THE HOLDING PERIOD

- The data suggests that real estate investors generally understand the value that proactively managing ESG risks and opportunities can bring to their properties.
- Dedicated internal or external experts review and implement action plans that are based on targeted pre-investment research.
- Scores are lowest for the smallest investors, potentially reflecting a lack of resources to develop and implement ESG value creation plans.

**Post-investment, how do you manage material ESG risks and ESG opportunities to create value during the holding period?**

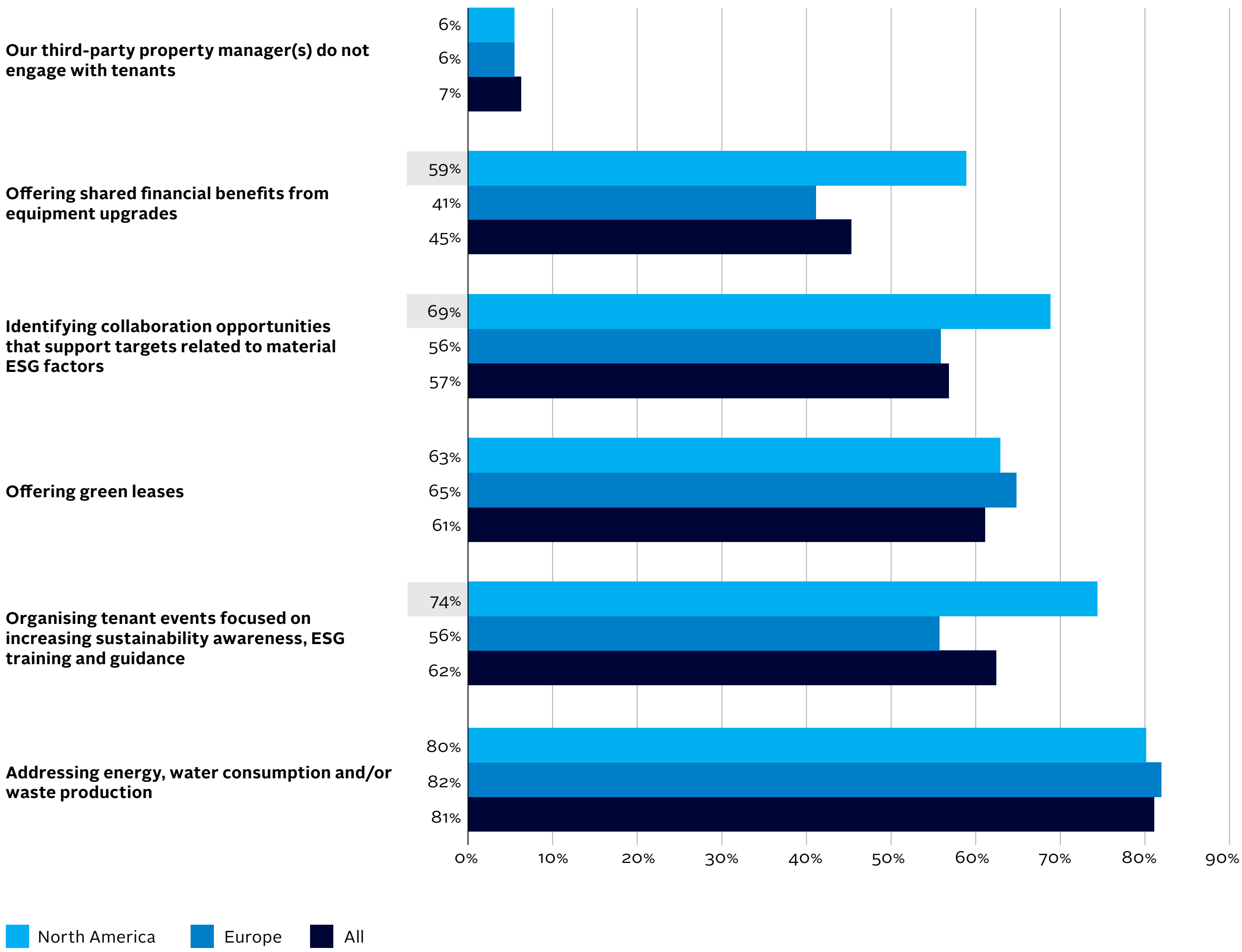



**Source**: Indicator RE 14. Denominator: 244 (real estate investors with >10% AUM in real estate)

# TENANT ENGAGEMENT EFFORTS FOCUS PRIMARILY ON REDUCING RESOURCE CONSUMPTION

- A significant majority of property managers engage with real estate tenants on reducing energy, water consumption, and/or waste production, highlighting a strong focus on environmental sustainability.
- More than half offer green leases, integrating environmental considerations directly into rental agreements, which suggests that they are seen as effective tools for incentivising action.
- North America, even though on a much smaller signatory base, is particularly noteworthy for identifying collaboration opportunities that support ESG targets as well as organising tenant events focused on increasing ESG awareness.

**How does your third-party property manager(s) engage with tenants?**

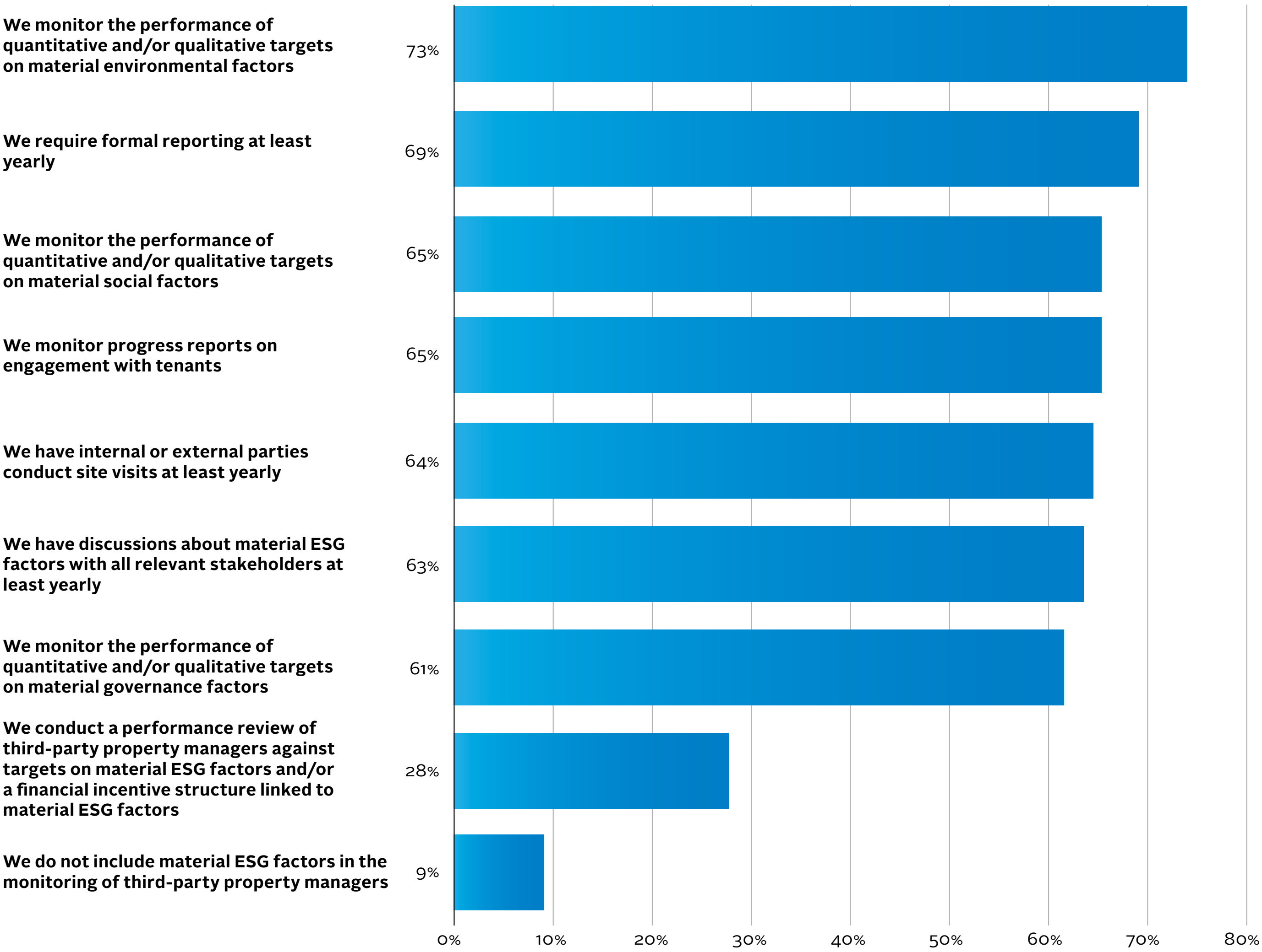



**Source**: Indicator RE 18. Denominator: 244 (real estate investors with >10% AUM in real estate). Denominator for Europe: 135. Denominator for North America: 54.

# MONITORING ESG PERFORMANCE OF THIRD-PARTY PROPERTY MANAGERS IS WELL ESTABLISHED

- The data suggests that investors generally seek to monitor the ESG performance of third-party property managers, most notably in relation to environmental targets.
- Only 28% of respondents conduct formal annual ESG performance reviews of their property managers and/or link ESG performance to financial incentives.
- The governance and alignment of relationships between property managers and investors could be strengthened in relation to ESG.
- Clear targets and formal review may help ensure better understanding among property managers of the importance of ESG to investors, while tying ESG performance to financial incentives can be an effective tool to better align each organisation's actions and priorities.

**How do you include material ESG factors when monitoring current third-party property managers?**

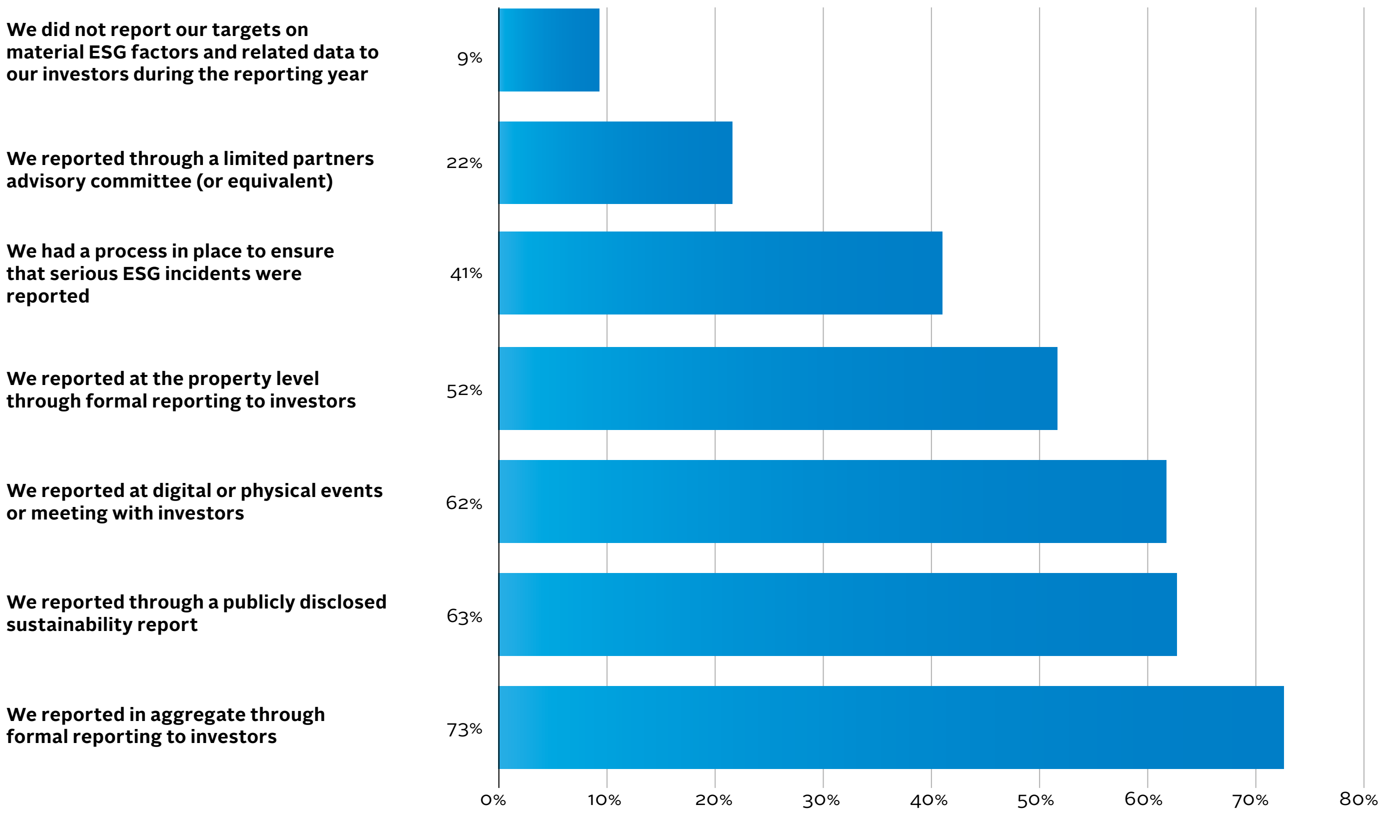



**Source**: Indicator RE 8. Percentages are based on the number of signatories who answered the particular question. All sub-questions have a denominator of 183.

# REPORTING ON MATERIAL ESG FACTORS IS THE NORM

- ESG reporting is well-established among real estate signatories: only 9% of respondents do not report on ESG targets and related data to their investors.
- Reporting appears to be more common in aggregate rather than at the individual property level, making it easier to assess and compare ESG performance across funds/strategies.
- Clients/beneficiaries may not have a full view of key ESG risks given lower responses indicating property-level reporting and reporting of serious ESG incidents.

**During the reporting year, how did you report on your targets on material ESG factors and related data to your investors?**




**Source**: Indicator RE 21. Denominator: 244 (real estate investors with >10% AUM in real estate)

## CREDITS

### AUTHORS:

Anna Shaikly
Simon Whistler

### CONTRIBUTORS:

Bhushan Varadkar
Eilidh Wagstaff

### EDITOR:

Casey Aspin

### DESIGN:

Christopher Perrins

### The Principles for Responsible Investment (PRI)

The PRI works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

More information: www.unpri.org

PRI Principles for Responsible Investment

## The PRI is an investor initiative in partnership with UNEP Finance Initiative and the UN Global Compact.

### United Nations Environment Programme Finance Initiative (UNEP FI)

UNEP FI is a unique partnership between the United Nations Environment Programme (UNEP) and the global financial sector. UNEP FI works closely with over 200 financial institutions that are signatories to the UNEP FI Statement on Sustainable Development, and a range of partner organisations, to develop and promote linkages between sustainability and financial performance. Through peer-to-peer networks, research and training, UNEP FI carries out its mission to identify, promote, and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations.

More information: www.unepfi.org

UN environment programme | finance initiative

### United Nations Global Compact

The United Nations Global Compact is a call to companies everywhere to align their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption, and to take action in support of UN goals and issues embodied in the Sustainable Development Goals. The UN Global Compact is a leadership platform for the development, implementation and disclosure of responsible corporate practices. Launched in 2000, it is the largest corporate sustainability initiative in the world, with more than 8,800 companies and 4,000 non-business signatories based in over 160 countries, and more than 80 Local Networks.

More information: www.unglobalcompact.org

United Nations Global Compact