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# Real Estate Predictions 2021

## The Impact of Social Good on Real Estate

**ESG as a value driver for real estate**

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"ESG", the generally used acronym for "Environmental, Social and Governance", has become an important business consideration all around the world. For instance, real estate investors have an increasing focus on sustainability. However, ESG in real estate can be so much more impactful. How can it become an important value driver?

### ESG and real estate

Once upon a time, real estate embodied the epitome of capitalism. The trend, however, is growing quite the opposite way. The application of ESG standards on real estate (notably by governments and developers in many developed countries) has shown that this asset class is also relevant when these guiding principles are being applied. Awareness is growing that real estate can have a significant social impact either through the form of rehabilitation of public spaces (indirectly attributing value to existing real estate), affordable housing, social housing, and care centers, or through an environmental focus investment on new buildings such as green buildings.

### Vital for investors

The correlative appetite that investors have for ESG, closes the loophole where more (long term) value is attributed to real estate assets. Medium-to-long term profit is therefore considered and kept with the usual lower risk volatility of a real estate asset. Sustainability has become increasingly vital to real estate investors. This is evident from the development of the Sustainability guidelines of the European Association for Investors in Non-Listed Real Estate Vehicles ("INREV")[1] to also adhere to investors' needs. Another indication is the increased participation in the 2020 GRESB real estate assessment. This is the investor-driven global ESG benchmark and reporting framework for listed property companies, private property funds, developers and investors that invest directly in real estate[2] ESG is therefore here to stay and will increasingly shape and influence real estate valuation, and therefore real estate investment, as investors wish to allocate their commitments under this banner.

### Impact on the community

However, the impact of ESG on the real estate industry goes beyond what is mentioned above. ESG, aside from fostering eco-friendly buildings, also allows space to include considerations about the impact of properties on the community, covering aspects like diversity. The real estate industry must respond to this challenge by creating opportunities through social impact investing, like multi-tenant shared spaces or the transformation of underutilized buildings into enthusiastic venues. In practice, the major obstacle is that investors will need to reinvent their traditional investment models to match the needs of the local community.

### ESG and infrastructure

Obviously, real estate and infrastructure are closely related. For example, the real estate industry is a major consumer of energy. Therefore, the construction of more sustainable buildings, e.g. by means of new eco-friendly materials or smart technological heating or ventilation, not only helps the environment, but it also boosts the return of the respective real estate investment, improving investment performance. Governments around the world are increasingly fostering these new construction methods to improve the carbon print of cities and emissions mitigation. As such, it is also relevant to take a quick look at the impact of ESG in infrastructure.

### Overcoming new infrastructural challenges

Implementing an efficient ESG-focused infrastructure system is vital for undeveloped countries – it provides access to the most basic services like energy and water for the community. Also, for developed countries, it may help to face new challenges, such as the increase of population in urban areas and the environmental concerns. Additionally, ESG standards are already proving to be decisive in infrastructure closings. This is because investments are beginning to face community oppositions, which is often due to the lack of ESG considerations, resulting in costly delays or changes to the initial project.

"Sustainability is here to stay or we may not be"

**Niall FitzGerald**

### Smart cities

Another expression of the ESG impact on infrastructure is the so-called "Smart cities" initiative, which refers to urban areas for which different innovative technological methods are designed. The output generated by such methods (e.g. in the form of data or statistics) can assure that city infrastructure is managed and organized more efficiently. Most of these methods are nowadays designed to allow ESG guidelines to span across the life of a city, in the respective assets, community services and resources, including better (and greener!) transportation, improved communication networks, optimization of energy consumption, water supply, crime detection and waste.

1 https://www.inrev.org/guidelines/module/sustainability#inrev-guidelines
2 https://gresb.com/2020-real-estate-results/

### Some examples: Dubai, Singapore, and Luxembourg

A successful example of a smart city is Dubai[3], which is tech-innovative in various sectors. A few examples:

- **transportation:** development of the first hyperloop between Dubai and Abu Dhabi and of autonomous air taxis
- **tourism:** project Oasis Eco Resort which aims to build a sustainable complex in the middle of the desert
- **housing:** project Martian city aimed at build houses in the desert for 600,000 people as a start for a 100-year Mars colonization plan
- **energy:** a mega solar park with the aim of making Dubai an eco-friendly powerhouse
- **security:** development of self-driving police cars.

Singapore is also a pioneer in this field. It has introduced the broader concept of smart nation[4]. Some examples of ESG tech innovations in Singapore are the development of a cashless public transport, the digital engagement and transformation of healthcare ("Telehealth"), the development of a platform used as a channel between schools and parents ("Parents Gateway"), and the development of "Lamppost as a Platform", i.e. a project which aims at maximizing the use of street lampposts to monitor changes related to environmental conditions, installation of cameras to analyze crowd build-ups and better monitor to increase safety in public spaces.

Finally, Luxembourg is also moving towards the concept of a smart nation. For a more specific analysis on the digital innovations on our jurisdiction, please see Deloitte's article on this topic[5].

### The backlash from COVID-19

It is relevant to understand how these concepts will develop in the midst of a worldwide pandemic. There is no doubt that the current pandemic has so far has affected how stakeholders look at vested assets and has slowed down further (real assets) investing. COVID-19 has severely impacted real estate valuations. Due to the lockdown, site visits were hampered. At the same time, many transactions were put on hold as this pandemic seems to be shifting people's demands for use of real assets, such as an increase in the search for bigger houses with gardens outside the urban areas, due to working from home). As much as the pandemic has slowed down economies and the real estate industry activity, the positive side of it is the wake-up call for investors to prioritize sustainable investments.

### The environmental factor

In particular, COVID-19 has brought out the environmental factor by enhancing the urgent global need to decrease pollution and improve precarious sanitation systems. In fact, the initial slow start of the adoption of ESG standards was probably built on the erroneous perception focusing on positive social impact would reduce financial return. It is becoming evident that it is indeed the opposite.

3 https://scgn.smartdubai.ae/
4 https://www.smartnation.gov.sg/
5 https://www2.deloitte.com/lu/en/pages/public-sector/articles/luxembourg-towards-smart-nation.html

### The social factor

However, the major spotlight is on the social factor: COVID-19 seems to be reshaping how the community should interact and behave from now on, which also calls for a revaluation of the current transport, technology and health infrastructures. This said, more than ever, it is key that millennial investors - as well as governments - not only focus on traditional financial metrics but also on their ESG performance in order to create a positive long-term impact.

### Recent global developments

This reality brings us also to the consequent topic of a global increase of guidelines and regulations related to ESG investments. The United Nations have outlined 17 sustainable development goals in the UN 2030 Agenda for Sustainable Development, which must be achieved for a more global sustainable future. Also, these goals represent the current challenges worldwide: poverty, inequality, climate change, environmental degradation, peace and justice[6]. By adopting the Paris Agreement on climate change[7] and the UN 2030 Agenda for Sustainable Development, the European Commission developed an Action Plan in March 2018 on different measures regarding financing sustainable growth[8].

### Transparency

As part of the Action Plan, Regulation (EU) 2019/2088 on sustainable Finance Disclosure regulation (SFDR) was published, which aims to provide more transparency on the degree of sustainability of financial products, to channel private investment towards sustainable investments while preventing green washing[9]. Its phase-in implementation will start on 10 March 2021. As a complement of this Regulation, the European Supervisory Authorities have developed a Joint Committee draft Regulatory Technical Standards (RTS) on ESG disclosures, for which a Consultation Paper was published in April 2020, seeking input on proposed ESG disclosure standards for financial market participants, advisers and products[10]. Luxembourg is already taking relevant steps in this respect, such as the recent CSSF communication issued on 16th December 2020 on regulatory requirements and fast track procedure in relation to the SFDR Regulation[11].

### European Commission

Also as part of the Action Plan, last November the European Commission launched a public consultation[12] on some of the criteria for determining which economic activities can qualify for the classification system for sustainable economic activities under the European Taxonomy Regulation[13] that focus on climate change mitigation. Furthermore, the European Union published a Directive back in 2014, which requires big companies to disclose certain information about how they operate and manage social and environmental challenges[14].

### More developments

Another recent development is the fact that there are countries that already officially recognize that climate change represents economic uncertainty and risk. One of them is the US, where the Federal Reserve included climate change in their list of financial stability risks (including real estate) in the Financial Stability Report of November 2020.[15] Some countries are exploring the green bonds market, such as Luxembourg and Germany. In this respect also note that the European Green Deal Investment Plan of 14 January 2020 announced that the Commission will establish an EU Green Bond Standard (GBS).[16] Finally, the European Union is currently reviewing the regulation for the collective investment vehicle, the European Long Term Investments Funds ("ELTIFs"). ELTIFs are funds that attract institutional and private funding to channel their investments into long-term assets, including real estate assets such as nursing homes, schools, prisons, and social housing. As such, ELTIFs can be a vehicle to enhance the access to ESG-focused investment.[17]

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6 https://sustainabledevelopment.un.org/post2015/transformingourworld
7 https://unfccc.int/sites/default/files/english_paris_agreement.pdf
8 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097
9 https://eur-lex.europa.eu/eli/reg/2019/2088/oj
10 https://www.esma.europa.eu/sites/default/files/jc_2020_16_-_joint_consultation_paper_on_esg_disclosures.pdf
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12 https://ec.europa.eu/commission/presscorner/detail/en/mex_20_2176#3
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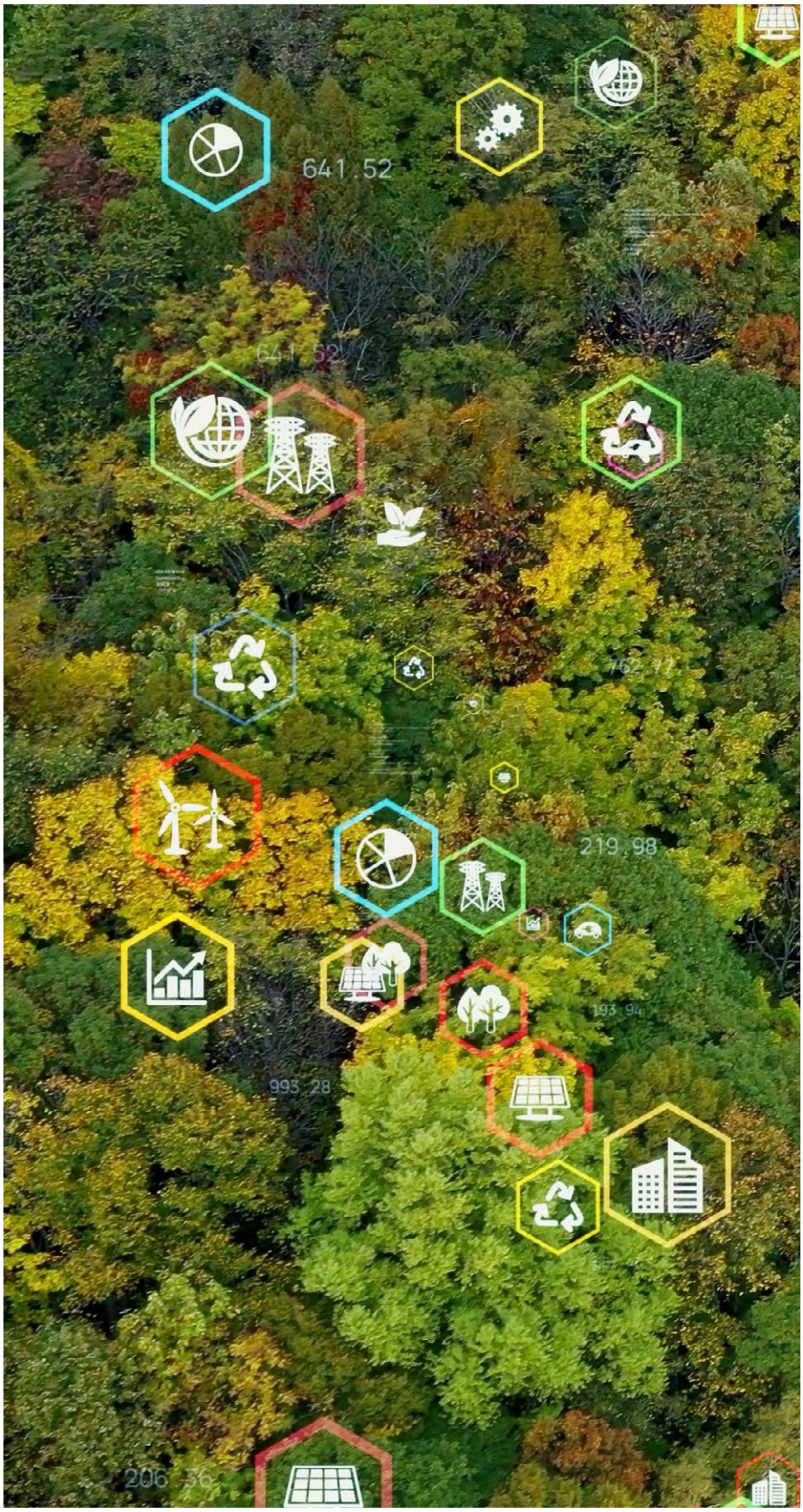
15 https://www.federalreserve.gov/publications/files/financial-stability-report-20201109.pdf
16 https://ec.europa.eu/commission/presscorner/detail/en/fs_20_48
17 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32015R0760

## A successful "sustainability-proof" business

This said, it is expected that the regulation around ESG should continue to increase in detail. Investors will probably be impacted by ESG-related legal and regulatory disclosures, for which proper advising from experts may be needed. Also, there is no doubt that the global real estate market is already aware that ESG principles are key for sustainable investments. In fact, sustainable investing could soon become the standard way of investing. In order to achieve this, real estate investors should ensure that the fund management is aligned with their intended positive social impact. At Deloitte we are looking forward on embarking on this journey with our clients to achieve a successful "sustainability-proof" business.

**Authors**
**Francisco Da Cunha**
**Partner | Tax M&A | LU**
fdacunha@deloitte.lu

**Filipa Belchior Coimbra**
**Assistant Manager | Tax M&A | LU**
fbelchiorcoimbra@deloitte.lu



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