

UK Cross Sector – November 2021

Q
SPOTLIGHT
Savills Research

Real Estate and the Carbon Challenge



The Investment and Policy Landscape

A full-page background image of a lush green forest. Tall, thin tree trunks rise vertically, creating a sense of height. The canopy is thick with bright green leaves, and sunlight filters through in dappled patterns across the forest floor. A narrow, light-colored path leads from the bottom right towards the center of the image.

“Unlocking investment is a key issue for the real estate industry as it aims to reach its own sustainability goals”

Welcome

This year's Conference of the Parties (COP26) in Glasgow is a milestone event for the world to address the challenge of climate change. As well as setting targets to reduce emissions and protect ecosystems, COP26 is turning to the issue of finance to deliver these climate goals. With developed countries tasked with mobilising at least \$100bn in climate finance per year, it is clear that finding ways to finance the transition to net zero will become a primary concern for the global economy in the coming years.

Policy needs to focus not only on public sector action, but also on harnessing private finance in pursuit of carbon reduction. Over £50bn of commercial investment flows into UK real estate every year, but a lack of data, transparency and consistent government policy is preventing sustainable investment reaching the levels required to decarbonise the sector.

Encouragingly, there are signs occupiers are willing to pay more for energy efficient buildings in some sectors, driving a green premium, while growing understanding of embodied carbon measurement will help the credentials of older stock. But residential and retail property are likely to prove the most challenging areas to green, and require greater policy intervention than has been seen so far.

Reducing carbon emissions, like other aspects of the wider ESG agenda, is often framed in terms of risk, stranded assets and the high cost of achieving carbon neutrality. But the scale of change needed will present savvy investors with new opportunities, and investing in green property does not necessarily mean sacrificing returns.

At Savills UK, we reduced our scope 1 and 2 carbon emissions from the UK offices in 2020 by 36%. But there is still significant work to be done. We welcome the opportunity COP26 will provide to refocus on decarbonisation after the disruption of the last 18 months, and trust that you will find this *Spotlight* helpful as you consider your own strategy.



Richard Rees

UK Managing Director

+44 (0) 207 016 3726

rrees@savills.com

Is commercial easier to green?

We look at the key reasons why making commercial property more environmentally sustainable is less of a challenge than it is for residential stock

A large proportion of the commercial stock in the UK requires further investment to become environmentally sustainable – 87% of the office stock in the UK's major office markets has an EPC rating of C or below. However, there are a number of reasons why this should be less of a challenge than doing the same for residential property. These include:

■ **Size** – Not only is the commercial property sector much smaller than the residential one, but the size or value of individual assets is generally larger. This means that fewer decisions and interventions will be needed to improve the stock in the office and logistics sectors.

■ **Ownership** – The majority of commercial property is owned by either corporate or institutional investors. Most of these investors have their own Environmental,

Social and Governance (ESG) targets and thus will be making the changes that need to be done in line with or, in some cases ahead of legislative changes.

■ **Re-investment** – Investors in commercial property have always factored in the costs of obsolescence to ensure that their asset remains lettable at the best market rates in the future. This means that in certain parts of the market, for example City of London offices, up to half of the entire stock has been refurbished or redeveloped in the last 20 years.

Our research shows that while there may not be a guaranteed green rental premium in the office market, you are 70% more likely to achieve a top decile rent if your building has a BREEAM rating of Very Good or better.

■ **Understanding** – With labelling systems such

as BREEAM and LEED becoming increasingly common throughout the last 20 years, a rising proportion of all new build stock has been built to these standards. This trend continues, with 44% of central London office developments that started this year targeting a BREEAM rating of Very Good or above.

■ **Financeable** – The rise in availability of green debt and equity and the evidence that already exists that greener buildings cost less to run, means that there is less persuasion (or government investment) needed to make the commercial property stock more sustainable.

THE CHALLENGE REMAINS THE OLDER STANDING STOCK

In common with the residential sector, there is still a large proportion of the commercial property stock in the UK that needs further investment as figure 1 shows.

Offices

Rising costs of mitigating obsolescence will be a challenge, but not an insurmountable one

The bulk of both the existing and planned office space in the UK is owned by professional investors, most of whom are aware that they have to invest in keeping their assets lettable. While there are challenges that owners face in terms of the ability to influence the behaviour of their tenants, we expect to see this becoming less of an issue as EPCs give way to measures that monitor actual energy usage such as DEC or NABERS.

Tenant demand is already rising for greener office buildings, and 45% of all central London office lettings since 2018 have been on space with a BREEAM rating of Excellent or better. The bigger challenge might be on the supply side, with only 44% of the planned development completions over the next three years aiming for a similarly high rating.

However, an undersupply of the greenest space might not be a bad thing at this time, as it will push up rents and thus firmly prove that there is a “green premium”.

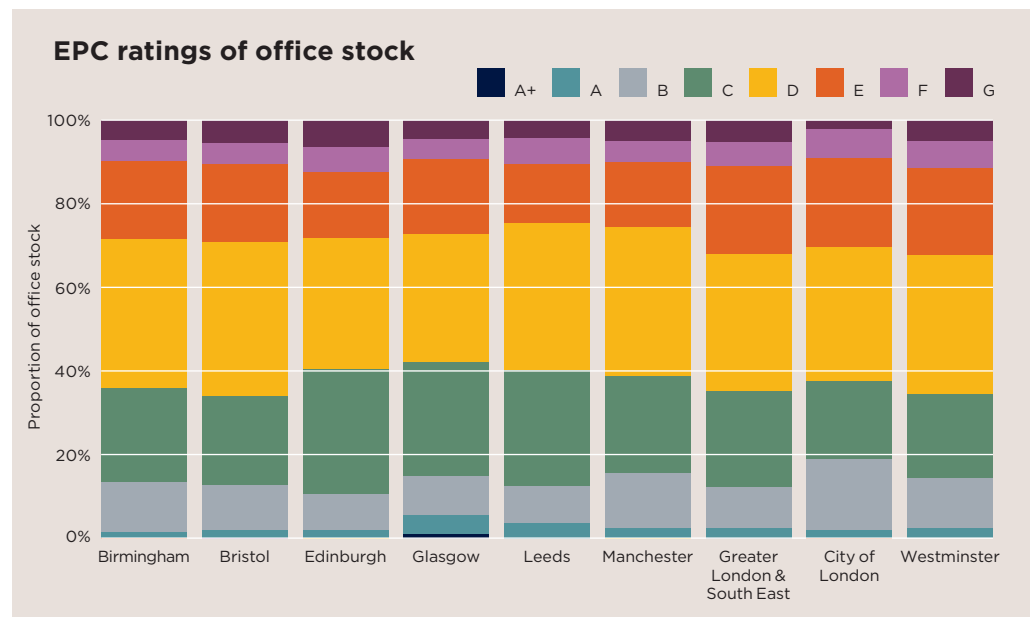


figure 1

Source Savills Research

45%
of all central London office lettings
since 2018 have been on space with a
BREEAM rating of Excellent or better

💡 87% of the office stock in the UK's office markets has an EPC rating of C or below 💡

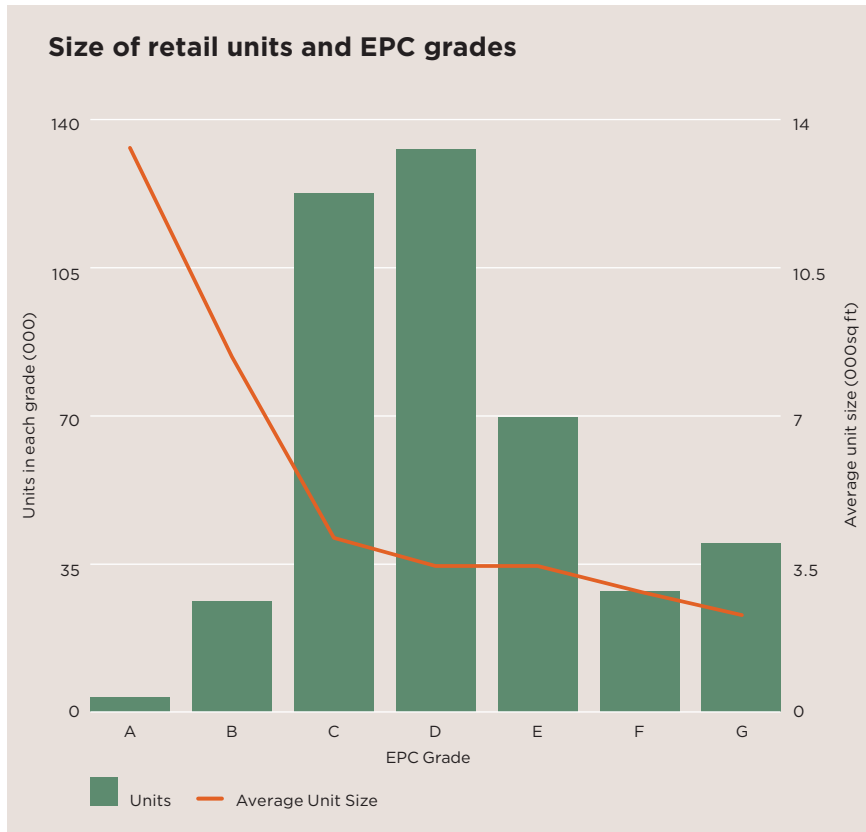


figure 2

Source Savills Research

Retail

Small units and fragmented ownerships present a challenge

What needs to be done to get retail property to be carbon neutral? British shops emit over 8 MtCO₂e more than the emissions targets derived from current Building Regulations. Ambitious targets to decrease carbon footprints through the Minimum Energy Efficiency Standards (MEES) mean that 185 million sq ft of retail outlets may be unlettable by 2023. To meet the minimum B grade standards being considered for 2030, 1.4 billion sq ft (83% of stock) will need to be improved. This will come at a considerable cost and in many cases may not be economically viable. So who pays for it?

For large institutional landlords, ESG obligations and lettable space will be key drivers in reducing outlet emissions. The size of their individual investments and access to capital will increase viability. However, most retail property emissions are not associated with shopping centres, retail parks and large high street blocks, which only account for around 25% of retail property emissions, the rest being from smaller

investors, largely in fragmented ownership.

Smaller ownerships, which account for the vast number of individual premises are often located in secondary and tertiary pitches and in smaller individual units. Small shops are more difficult to retrofit, or are much older and it is therefore little surprise that the average unit size of A-rated retail property is five times as large as G-rated properties. There is also a strong correlation between the worst performing assets and high retail vacancy rates, which begs the question in some instances whether bringing some shops up to grade will actually be worth the investment. Either way, it is shops outside of both key ownerships and core trading locations that are likely to require more government intervention, policy and support to drive the change.

185m sq ft
of retail outlets may be
unlettable by 2023

Logistics

Greater utilisation of rooftop solar could make the sector almost energy neutral

There is currently 583m sq ft of warehouse space in the UK in units of 100,000 sq ft and above, and by 2030 we estimate that this figure will rise to 832m sq ft. These units are typically large, single storey buildings with extensive roof space, offering a potential location to install rooftop solar panels that could provide green energy back to the occupier of the building and therefore reduce their energy requirement from the grid.

Working on the assumption that on average around 40% of a warehouse roof may be suitable for the installation of solar panels means we can therefore estimate how much energy could be created. Based upon this calculation, the additional 250m sq ft of warehousing due to be delivered in the next decade could deliver 1700 MW of energy, which is 97% of the total energy need from the new development.

Work to retrofit existing stock with rooftop solar may be challenging due to the weight-bearing capabilities of older units, but the potential for new build units to be energy neutral is clear.



97%

Rooftop solar could meet
nearly all the energy
requirements of new units

“Few sectors touch on so many of the UN’s sustainable development goals as farming, making it a prime opportunity for investors”

Green investment in land, food and nature

With net zero and wider sustainability agendas gathering pace, we look at how green investment can be leveraged against new and existing rural assets

Nature-based solutions are a major part of carbon neutral operational and investment strategies. However, alongside offsetting, the UK countryside has to balance existing and often competing services, from food production to renewable energy. The rural landscape will have to change as new services are accommodated and existing ones adapt to keep up.

RENEWABLE ENERGY

Renewable energy is a core opportunity for green investment in the rural economy. Currently, 27% of UK energy demand is supplied by renewables, meaning significant expansion is needed to reach net zero by 2050. Connecting to the grid can be costly, and energy storage solutions will be essential to smooth out the peaks and troughs of renewable supply. The government has signalled major investment in green technology in pursuit of net zero, so novel energy storage solutions are likely to become more commercially viable in the near future.

Making renewables a viable alternative to the current fossil fuel based system is not just a storage challenge though. At present, gas power stations have preferential access to the grid, which means that renewable energy suppliers must turn down their systems in periods of excess supply, such as when it is particularly sunny or windy. Addressing this bias against renewables is key to building investor confidence.

As renewables continue to mature, investment models will shift from areas of low competition or subsidy, to a more traditional model focused upon value creation. Accessing land for renewables will remain difficult, but as agricultural policy evolves to accommodate net zero objectives, more opportunities should be available at a viable scale.

FORESTRY AND OFFSETS

Competition for existing forestry and for land suitable for tree planting has never been greater. On the one hand, external investment in meeting the government’s ambitious tree planting targets is very welcome. On the other, the rapid fuelling of demand and the associated rise in land values mean investors need to be clear about the returns these assets

will eventually deliver. The year to September 2021 saw a 60% uplift in average value per net productive hectare for s timber investments.

Why is the market for forestry so hot? Firstly, the traditional means of creating revenue through the harvesting and trade of timber remains buoyant. However, more new market entrants are seeking sustainability credentials, both in existing forests and new afforestation sites. Planting trees as a source of secure carbon offsets theoretically makes forestry both a financial and environmental investment.

But there is a growing distinction between commercial forestry and woodland assets managed for carbon. Formal carbon accreditation through the Woodland Carbon Code (WCC) requires new planting schemes to prove additionality, meaning that net carbon savings should be above those which would have occurred anyway. While some commercial schemes will qualify, additionality will need to be proven, for instance through enhanced environmental gain. The WCC therefore tends to produce more biodiverse and less commercially productive woodlands.

Consequently, commercial carbon and forestry schemes are increasingly incompatible. Why then are ESG-investors targeting forestry rather than just planting land? Even existing woodland can be actively managed to preserve or increase carbon sequestration, offering owners a quantifiable figure that can be used as an internal “inset” on a carbon balance sheet. The “value” investors derive from owning these assets appears to be a much more holistic term and places these assets outside the scope of purely financial returns.

Similar opportunities could be found through bringing more existing woodland back into management, as well hedgerow creation, landscape partnerships or peatland schemes. Partnering with farmers and landowners, rather than a direct acquisition model, may also help unlock opportunities as the supply of freehold opportunities is highly constrained.

FARMING: FOOD, FIBRE AND FUEL

Few sectors touch on so many of the UN’s Sustainable Development Goals as farming, but despite the presence of green credentials and counter-cyclical and counter-inflationary

characteristics, lower investment yields make agriculture less appealing than other property classes. Is all that about to change?

Most farmers will be focused on government announcements regarding the transition away from income support to providing services to the environment. Selling carbon stored in agricultural soils is the panacea many farmers are hoping for to replace lost CAP income, but like any farm asset, owners will need to ensure they have enough for their own needs before selling the asset to third parties.

However, the shift in carbon thinking should not be about just income, but also accountability. Any farmer seeking access to bank finance or insurance will have to start disclosing more environmental impact information, and institutions with land let to farmers will require the same information.

Farming must undertake a significant transformation to achieve net zero. The transition may present options for ESG-hungry investors to help deliver the infrastructure and technology needed on farms to reduce emissions. A note of caution for investors in land looking for formal carbon offsets is that verification of these offsets often requires permanent land use change. As political awareness of the impact of this on existing land use patterns increases, nature-based solutions that enhance, or at least don’t undermine, national food security and rural communities will become more valuable.

In terms of farming itself, methods that avoid reliance on chemistry and fossil fuels are needed. The regenerative agriculture movement and a tripling in the cost of artificial fertiliser since 2020 as a result of the gas price spike may be the nudges farmers need to embrace this. As supply chains increasingly switch to more sustainable sources for everything from medicines to plastics, there are multiple opportunities in the bio-economy for innovative growers. A contractual approach has been key to bringing niche crops into the mainstream in the past, and a coalition of like-minded growers would be the most powerful force for change while also ensuring that farming communities are provided a ‘Just Transition’ in land-based activities.



“ 27% of UK energy demand is supplied by renewables, meaning significant expansion is needed to reach net zero ”

Residential journey to net zero

Over a fifth of UK CO₂ emissions are from residential stock, but it is also likely to be the toughest sector to decarbonise

The residential sector is responsible for over one fifth of all UK CO₂ emissions and since 2014 decarbonisation rates have slowed. Emissions of CO₂ have increased by 9% since 2014. In 2017 the government published an ambition to upgrade all homes where “cost efficient, affordable and practical” to EPC C by 2035. But the scale of the challenge is considerable, with a third of homes built pre war still carrying EPC ratings of E or below. To meet the 2035 target, the rate of retrofit needs to be seven times greater than current levels and EPC improvements data suggests the total cost could be as much as £330 billion.

The problem will be harder to resolve than other sectors. Decarbonisation works are intrusive for residents, can impact the appearance of a home and may not result in lower energy bills. There is also currently limited evidence of a residential green premium that could incentivise improvements. Consequently, a higher level of policy intervention such as property specific taxes will likely be needed to move the market, particularly for owner occupiers.

AMBITIONS AND CHALLENGES

- In 2017 the government published an ambition to upgrade all homes where “cost efficient, affordable and practical” to EPC C by 2035 (EPC E by 2020 and EPC D 2025)
- To meet the 2035 target, the rate of energy efficient renovation will need to increase by 7x according to the Department for Business, Energy and Industrial Strategy
- Information on EPCs estimates the cost of implementing all potential energy efficiency improvements is in the order of £330bn; previous grant schemes have been a drop in the ocean

Other policy considerations

HERITAGE PROPERTY

Listed properties present a particular challenge as improvement works will often conflict with the need to protect their special architectural and historical merit. Clarity on the policy trade off between heritage and energy efficiency is essential, including the nature of concessions and exemptions.

HEATING

While the International Energy Agency has already called for a ban on the sale of fossil fuel boilers by 2025, current government proposals are that they will only be banned on newly constructed homes from that date. A requirement for hydrogen ready boilers from 2035 looks more likely. Other alternatives such as heat pumps and biomass-fed district heating are likely to become increasingly common, subject to cost and production.

CARROTS & STICKS – THE ROLE OF TAXATION

Grant and green finance initiatives alone are unlikely to facilitate the step change in investment in energy efficiency needed to meet government targets. More radically, discounts and surcharges on property specific taxes such as stamp duty and council tax have the potential to increase the “green premium” and “brown discount” of housing, providing a greater incentive for owners to invest in energy efficiency improvements.

The challenge by tenure

AFFORDABLE HOUSING

- 5.08 million homes
- EPC ratings 2016-2020:
 - 54% A, B or C
 - 9% E, F or G
- Getting to zero carbon by 2050 is underpinned by regulatory requirement of the Decent Homes Standard
- SAVILLS HOUSING SECTOR SURVEY 2021
 - 25% of providers do not have a planned timescale to upgrade stock to zero carbon
 - 42% plan to complete works between 2031 and 2040
 - A further 19% plan to complete works between 2041 and 2050
 - 37% have not factored costs into their business plan
 - Average expected costs of improvement stand at £20,600 per dwelling
 - 17% of homes may be uneconomic to upgrade, a catalyst for redevelopment, stock sales and offsetting

£330bn

is the estimated cost of implementing all potential energy efficiency improvements

30%

of homes built pre war still carry E, F or G EPC ratings, rising to 47% for those built pre 1947

PROBLEM #1

The payback on many energy improvements remains **unattractive** (especially the big ticket items such as photovoltaics, solid floor and wall insulation).

THE ECONOMICS OF GETTING THE EPC LEVEL C:

Current EPC rating	% of homes	Estimated cost of works	Energy cost saving pa	Simple payback period
D	47%	£6,472	£179	36 years
E	10%	£13,285	£594	22 years
F & G	3%	£18,858	£1,339	14 years

Source English Housing Survey

PROBLEM #2

While the value of the asset is affected by its energy efficiency, the uplift in value for most homes won't justify the expenditure.

AVERAGE £ PER SQ FT V A BAND D HOME:

EPC A	EPC B	EPC C	EPC D	EPC E	EPC F	EPC G
+10%	+11%	+2%	0%	-2%	-6%	-15%

Limited value uplift

Value uplift at the extreme

Source DLUHC, HMLR

PRIVATE RENTED SECTOR

■ 5.57 million homes

■ EPC ratings 2016-2020:

39% A, B or C 18% E, F or G

■ In England and Wales private landlords already need to be at a minimum of EPC E unless costs exceed £3,500

■ Proposals are to tighten that to EPC C and to increase the exemption cost to £10,000

■ There are similar regulations in Scotland

■ As the ambition to reduce emissions increases, so minimum standards will be increased and exemptions tightened

■ These requirements will place an additional cost burden on private investors, putting particular pressure on mortgaged buy-to-let landlords. Institutions with purpose-built portfolios are much better placed to meet these obligations though currently represent less than 3% of the sector

OWNER OCCUPIERS

■ 18.93 million homes

■ EPC ratings 2016-2020:

38% A, B or C 21% E, F or G

■ Average energy consumption among owner occupiers is 21% higher than private renters and 43% higher than those in the affordable housing sector (Source: BEIS)

MORTGAGED

■ 8.70 million homes

■ Favoured policy lever is to tackle energy efficiency through mortgage lending or re-mortgage

■ That would involve lending targets for both energy efficiency improvements and the efficiency profile of a lender's portfolio

■ Were proposals to affect lending terms this could quickly change the economics of undertaking improvement works; particularly if interest rates rise

OUTRIGHT

■ 10.23 million homes

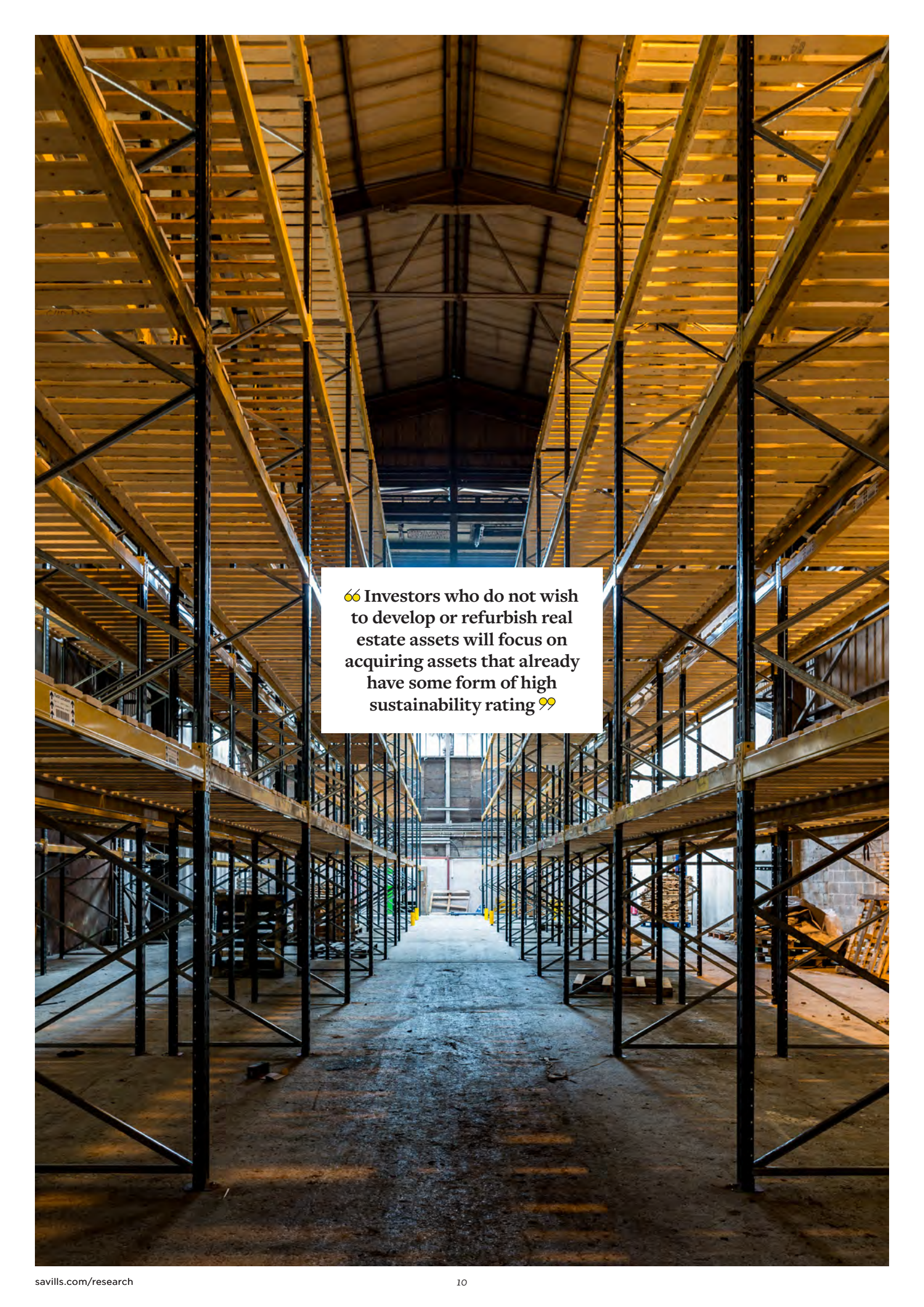
■ +1.55m in the past 10 years

■ Dominated by older households in less energy efficient homes

■ Owners are conscious of heating prices, but the cost of improvements presents a major obstacle unless increased grants plug the gap

■ Without a mortgage, the trigger point will often be on sale. Yet, on average, an outright owner has been in their home for 24 years.

THE
GREATEST
CHALLENGE

A photograph of a large, empty industrial warehouse. The space is filled with rows of tall, metal shelving units that stretch into the distance. The ceiling is high and features a complex network of steel beams and trusses. The floor is a smooth, light-colored concrete. The lighting is warm and even, highlighting the structural details of the building.

“ Investors who do not wish to develop or refurbish real estate assets will focus on acquiring assets that already have some form of high sustainability rating ”

“The best opportunities to buy green standing assets will be in the central London office market and Build to Rent market outside the capital”

How does this affect strategies for green real estate investors?

Increased consideration for environmental and social returns means that investors will need to take a broader view of what constitutes a green premium

GREEN PREMIUMS AND ENVIRONMENTAL RETURNS

Real estate investors will always want to make money from their investments. However, we do expect to see more consideration of environmental and social returns in the future, rather than just total returns. Investors will need to take an increasingly broad view of what constitutes a green premium, whether they are paying for it or creating it themselves. Criteria to be considered include:

■ *Lower energy costs* as an enabler for higher rent payments.

■ *Better buildings* will offer more than just being “greener”, and better always attracts a premium.

■ *The branding* impacts of a greener building, while less tangible, will be counted both by owners and tenants. Brand damage may become a concern.

■ *Carbon offset* costs will be higher for assets that are harder to decarbonise.

BUY GREEN OR BUILD GREEN?

Investors who do not wish to develop or refurbish real estate assets will focus on acquiring assets that already have some form of high sustainability rating. However, the comparatively slow pace of the delivery of such assets, particularly in the residential space, will mean that liquidity, competition and hence pricing of such assets will remain challenging.

In the commercial sectors we expect the best opportunities to buy green standing assets in the UK will be in the central London office market and in the residential Build to Rent market outside London.

Creating more sustainable real estate through refurbishment or development will continue to be the higher risk and higher return area of the property market. The increasing availability of cheaper debt for such projects will, to some degree, compensate for some of the higher capital expenditure involved. However, a bigger challenge to this strategy might be the inevitable rise of embodied carbon measurement and costing.

We believe that over the next decade it will become harder for developers to justify demolition and new construction, both in terms of their own ESG commitments, and through new planning policy. However, until an industry standard measure for the amortisation of embodied carbon has emerged it will be equally hard for investors to justify holding older stock instead of redeveloping it.

WILL GREENER INVESTMENT STRATEGIES CONFLICT WITH OTHER MOTIVATORS?

While legislation will definitely lead all real estate investors towards more environmentally sustainable portfolios, some will choose to go further than others. In much the same way as the equity market has investors who will only focus on ethical stocks, real estate investors who only own assets that have the highest ESG

standards have also emerged. These investors will increasingly sell their investors a blended total return that will include considerations of environmental and social returns.

The challenge for such investors will come when a hot asset class that offers a high total return directly conflicts with other drivers. For example, at present a common theme in real estate investing globally is “beds, meds and sheds”. However, given our earlier comments around the challenges involved in greening the residential sector, the beds bit might be hard to achieve in a sustainable fashion. Furthermore, our analysis of the Display Energy Certificate data for the UK suggests that the second biggest CO₂ emitter per square metre is laboratories, which could also put a meds focus in direct conflict with an environmentally sustainable investment strategy.

Which property sector emits the most CO₂?

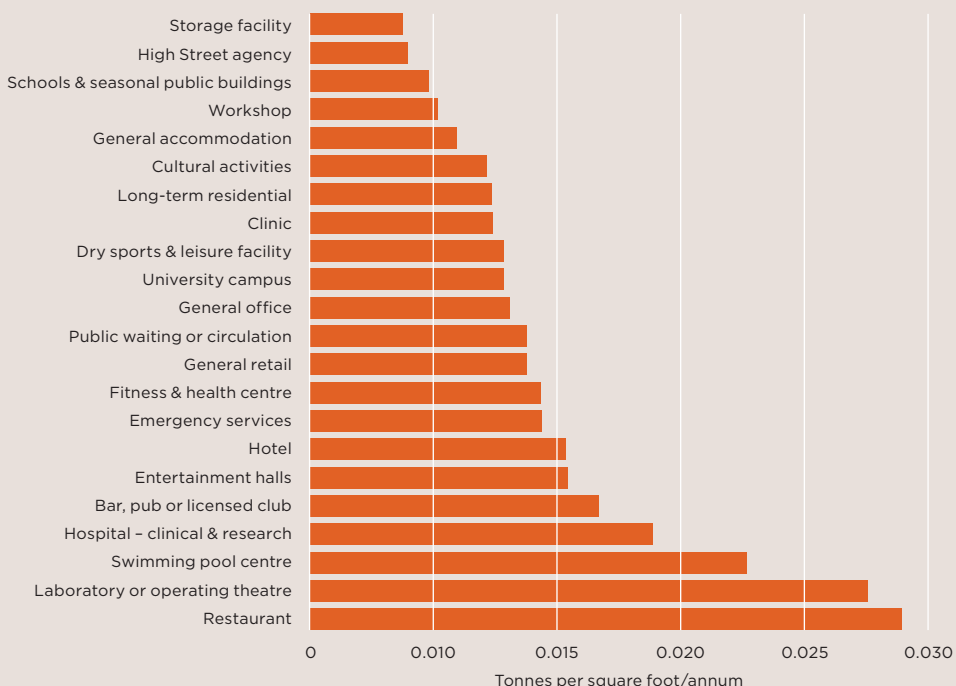


figure 3

Source Savills Research using DLUHC

“To develop the green finance market further, both industry and policymakers need to build on this idea of having greater transparency and openness”



Policy gaps and future requirements

Policy stability and long-term vision from the government is needed to enable the real estate industry to make a smooth transition to a low carbon economy

The UK government has developed plans to improve the energy efficiency of all buildings by mid 2035. However, there are significant gaps in the regulations and, to date, government policy has not provided the stability or long-term vision that will enable the industry to make a smooth transition to a low carbon economy.

CURRENT POLICY

Rather than setting sustainability requirements, policy efforts have been aimed at increasing retrofitting supply chains, capacity and encouraging innovation. However, there are still major barriers to retrofit, identified by

the UK Green Building Council, which apply across all sectors:

- High upfront costs, particularly for the newest technology
- A lack of finance mechanisms and a lack of a coherent offerings for institutional investors
- No fiscal incentives
- Limited loan and grant schemes that have prioritised specific measures and prevented a whole building approach.

The government's flagship scheme has been the £2 billion green homes grant launched in September 2020. As part of the government's 10-point plan, the green homes grant scheme was extended by £1 billion for a year after the initial programme became heavily over-subscribed, but was closed to new applicants in March 2021.

The scheme has been unable to mobilise the supply chain as planned. Oral evidence given to the Environmental Audit Committee from local authorities and industry bodies stated that the short-term nature of the funding would not give small retrofit providers

£5bn

of government development capital could unlock £100bn of private investment

2023

The year by which all privately rented commercial and public properties to be EPC E

sufficient confidence to scale up production. Coupled with delays in the funding vouchers being issued, the effect was for suppliers to retract due to ongoing uncertainty rather than expand capacity. To truly act as a catalyst, the scheme needed to be extended to provide a multi-year programme that would give suppliers the confidence to expand capacity. The same ethos should underpin all government efforts to deliver net zero goals.

DRIVING PRIVATE INVESTMENT IN DECARBONISATION

A similar critique of the wider UK policy landscape has been made by the Green Finance Institute, which stated in December 2020 that it “has yet to provide the market signals required to scale supply chains, jobs and investment in zero carbon heating solutions”. The same theme emerges in the Sixth Carbon Budget pathway document, with the first policy recommendation being to set a clear direction and standards for decarbonisation.

To develop the green finance market further, both industry and policymakers need to build on this idea of having greater transparency and openness. Proposals from the Green Finance Institute include reviewing the Standard Assessment Procedure to fairly reflect the benefits of new technologies in homes, and developing common benchmarks to facilitate accurate reporting to showcase relative performance of Green REIT portfolio assets. A standardised methodology and data framework for Building Renovation Passports is needed from government to build investor confidence and encourage more private money to fund retrofit programs.

Government could also play a stronger role in providing backing for private investors through national development banks, an approach that has been successful in Germany and the Netherlands. The OECD estimates that credit guarantee schemes can bring in £5-10 of private capital for every £1 of public capital over a five to 10 year timeframe. Similarly, the UK100 campaign Financing Local Energy proposes a National Net Zero Development bank and demonstrates that £5bn of government development capital could unlock £100bn of private investment.

2035

The year by which all owner-occupied homes should be EPC C rated

KEY DATES



RESIDENTIAL PROPERTY:

- Future homes standard for new build by 2025
- Fuel poor and rented homes to be EPC C by 2030
- Owner-occupied homes to be EPC C by 2035.



RENTED COMMERCIAL AND PUBLIC BUILDINGS:

- All privately rented properties to be EPC E rated by 2023
- Proposal for non-residential rented buildings to be EPC B by 2030, assuming upgrades are cost effective

REGULATORY GAPS

- 15.5 million owner-occupied homes are not currently covered by proposed efficiency standards
- Commercial buildings that are owned, not leased, are not covered by current policy proposals
- High carbon fuel phase outs is focused on coal and oil, but excludes heating powered by natural gas

Conclusions

If the UK real estate sector is to achieve the targets currently being set for energy efficiency and carbon consumption, policy needs to develop in several key areas:

1 A consistent road map is needed that sets requirements across all sectors, not just certain tenures. This will create clear expectations, and encourage investors and occupiers to plan for long term change, while also making it more likely that green premiums or brown discounts will emerge and encourage behavioural change through market forces.

2 More support should be given to early adopters. Certain sectors, such as social housing, are expected to be the pilot for trialling decarbonisation across a portfolio, but policy does not address the risk this poses if new technology or processes do not perform as expected. An insurance guarantee scheme that would give investors and property owners confidence to invest in new retrofitting or clean energy generation technology without taking on untenable financial burdens if new technology or processes do not perform as expected.

3 There should be greater consideration of how the tax system could be used to support businesses and individuals to make the transition to net zero. New fiscal incentives could encourage home owners to undertake retrofit works, such as 0% VAT on energy saving products and materials, or stamp duty being linked to energy efficiency. Supporting low income households will be critical to maintaining public support for net zero.

4 The industry and government need to create clearer performance reporting requirements and a standardised data framework to draw increased private investment. There is considerable appetite from financial institutions to invest in decarbonisation, but more transparency around the performance of their investments would be needed to build scale.

5 Incentives and penalties within the energy sector could be further rebalanced in favour of renewables. The recently announced plan to shift green surcharges from electricity bills onto gas bills is an important step in making clean energy the cheaper choice. However, rebalancing preferential access to grid capacity at times of excess energy supply to renewable sources could give investors further confidence in this area.

6 As operational carbon emissions are reduced, embodied carbon will become an increasingly important consideration for regulators, developers and investors. A consistent carbon policy that sets targets and transparency requirements for new development will help investors manage risk. It will also give a consistent comparison point to assess whether it is more sustainable to hold and refurbish, or redevelop existing assets. This would also improve understanding and assessments of nature based carbon sequestration schemes.

7 A multi-year programme of government investment in retrofitting is needed to improve contractor capacity. Addressing the skills gap with incentives and support for green training programmes would serve a dual purpose by also helping with the levelling up agenda.

Savills Earth

Sustainability delivered through a real estate lens

Savills Earth brings together the expertise of more than 100 specialists to support and advise clients on their sustainability, energy and carbon strategies. This is against a backdrop of increased public interest in cutting carbon emissions, more regulation, the proposed green-led recovery post Covid-19 and the clear need for action on climate change, environmental protection and social wellbeing. The team is working with clients to develop strategies that turn sustainability targets and commitments into reality. It recognises that every client has different requirements whether it's an individual project or a national portfolio.

Sara Gough

Head of Savills Earth
+44 (0) 7805 808 753
sgough@savills.com

David Jackson

ESG Working Group Lead
+44 (0) 7967 555 796
djackson@savills.com

Energy Infrastructure

Nick Green

Head of Land and Rural
+44 (0) 7968 550 378
ngreen@savills.com

Net Zero

Chris Cummings

Director
+44 (0) 7971 884 228
chris.cummings@savills.com

Buildings & Design

Jarrod Griffiths

Director
+44 (0) 7816 071 909
jgriffiths@savills.com





“ Savills Earth brings together the expertise of more than 100 specialists to support and advise clients on their sustainability, energy and carbon strategies ”



Savills Research

We're a dedicated team with an unrivalled reputation for producing well-informed and accurate analysis, research and commentary across all sectors of the UK property market.

To view copies of our previous Spotlight publications, go to www.savills.co.uk/insight-and-opinion/

Rural Research

Emily Norton

Head of Rural Research

+44 (0) 7807 999 204

emily.norton@savills.com

Joe Lloyd

Associate

+44 (0) 7790 824 970

joe.lloyd@savills.com

Molly Biddell

Analyst

+44 (0) 7866 885 240

molly.biddell@savills.com

Residential Research

Lucian Cook

Head of Residential Research

+44 (0) 7967 555 418

lcook@savills.com

Emily Williams

Associate Director

+44 (0) 7971 880 389

emily.williams@savills.com

World Research

Paul Tostevin

Head of Department

+44 (0) 7792 793 575

ptostevin@savills.com

Commercial Research

Mat Oakley

Head of Commercial Research

+44 (0) 7774 267 538

moakley@savills.com

Clare Bailey

Director

+44 (0) 7972 000 108

cbailey@savills.com

Tom Whittington

Director

+44 (0) 7968 550 304

twhittington@savills.com

Kevin Mofid

Director

+44 (0) 7812 249 386

kmofid@savills.com