ESG – A tipping point for opportunity and obligation

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Foreword

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Head of Real Estate – Shoosmiths

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Foreword

Not so long ago, Environmental, Social and Governance (ESG) was not the priority for businesses that it is today. For many, it was an internal box ticking compliance exercise. It has now become a business-critical item high on boardroom agendas across the world and increasingly seen as an essential factor in investment decision making.

With COP26 fresh in the memory, the E element of ESG has gained the lion's share of headlines. But businesses are now also striving for a better understanding of the social impact of their products and services, as well as to institute clear governance policies around responsible corporate behaviour. The broad coverage of ESG is reshaping the way businesses operate and driving positive change in all areas of our lives. Businesses can no longer afford merely to pay lip service to their ESG motives and greenwash their activities – for fear of reputational risk, regulatory scrutiny or profit loss.

As the volume increases on ESG so does the difficulty in discerning deliverable actions from honourable intentions; fact from fiction. Who are the pioneering businesses leading the charge on ESG and what does progress look like at a practical level? Where are the incremental changes being seen and what lessons can we take from them?

In this, the first of a series of reports from Shoosmiths on ESG, we look across the three distinct components of ESG to get under the skin of what ESG means and seek to answer the question: how are shifting mindsets around ESG tangibly influencing business and market change?

I hope you enjoy it.

Kirsten Hewson
Head of Real Estate – Shoosmiths

Fundamentals – The growth of ESG

- *What are ESG principles?*
- *Where does it come from?*
- *Why does it matter?*

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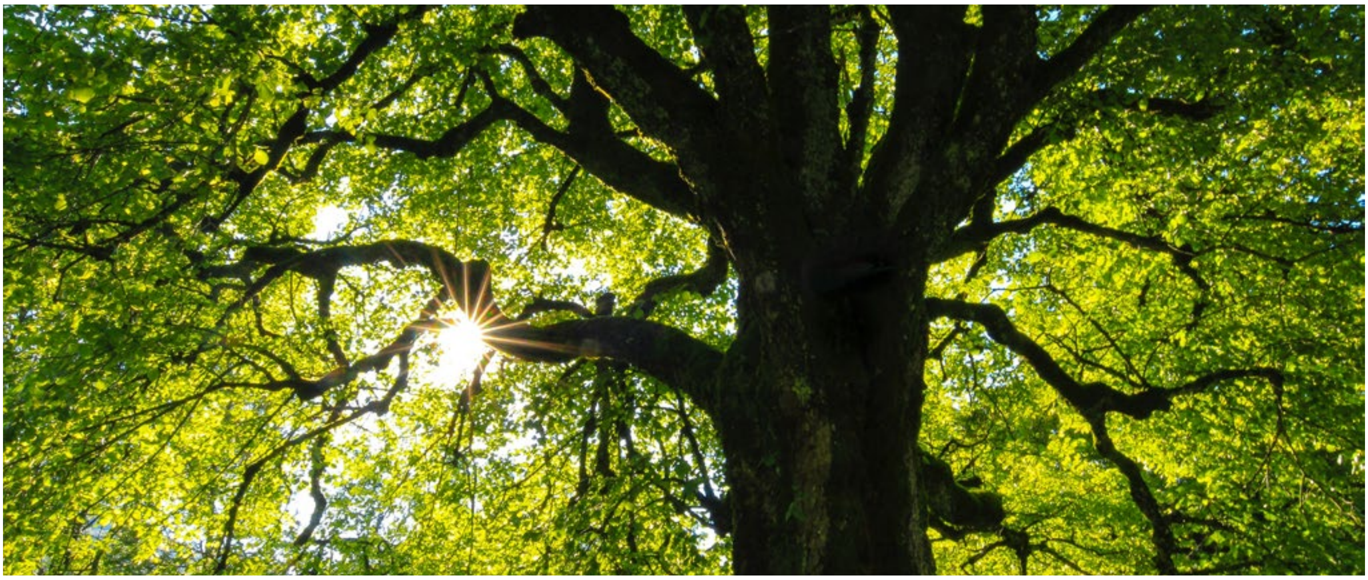
Fundamentals – The growth of ESG

ESG – Environmental, Social and Governance – has become shorthand for all that is good and green in innovation and industry. But what is it really about? What does it mean in practical terms? And, most importantly, are highly rated ESG credentials an optional add-on, a nice-to-have or fundamental to today's successful businesses?



Green shoots

The 'environmental' part is the most straightforward – anything a business does which impacts on the environment falls within this definition and affects its ESG credentials, for better or for worse. '**Environment**' comes first in ESG, and for good reason. We are living in a time of climate crisis, we are taking part in the race to net zero, and we need to live (and do business) sustainably to ensure availability of resources for future generations. Some businesses have a more obvious environmental impact than others – for example those operating in the UK's waste or water sectors, who are regulated by the Environment Agency or its cousins in the devolved nations. But all businesses use resources and have an environmental impact – whether that is electricity, gas, product packaging or travel – and the efficiency or otherwise of their deployment affects the business's ESG credentials.

Definitions of 'social' and 'governance' are less straightforward. There is no formal consensus about what these include and there is some cross-over between the categories.

'**Social**' broadly covers the relationship between a business and its human stakeholders – that is to say, employees, consumers and users of the goods and services it provides, and the community in which it operates. It encompasses traditional areas of legal regulation such as health and safety, human rights and modern slavery, as well as more vague concepts, such as community relations, business transparency and accountability.

'**Governance**' is perhaps the hardest to define. At a high level, it relates to the culture of the business, and the moral code by which it operates. It includes considerations of board structure and accountability, audit and management of corruption and bribery issues.

Back to the roots

ESG has its roots in the world of investment. Socially responsible investing (SRI) as a concept has been around for a very long time. As far back as the 1700s, North American Methodists and later Quakers eschewed investing in industries connected to the slave trade and in other businesses, such as the manufacture of alcohol and tobacco.

The term ESG was first used in a 2005 study entitled *Who Cares Wins* by the Global Compact, a joint initiative by financial institutions which were invited by the then United Nations Secretary-General, Kofi Annan, to take part. The difference between SRI and ESG, as reflected in the study, is that SRI is primarily about censorship (not investing in businesses which are perceived to do harm), whereas ESG is primarily about promoting good practice – on the basis that businesses with good ESG credentials are likely to be more successful and produce a better return on investment.

> “Increasingly, bidders need to offer value alongside evidence of good corporate citizenship.”

Tender carrots

Businesses seeking funding and investment, and those looking to contract with (in particular) government bodies are increasingly required to demonstrate their ESG credentials in order to be considered eligible.

Businesses with demonstrably good ESG strategies have access to a greater range of financial products and will appeal to a broader range of investors. There is an ever-increasing number of institutional investors and funds which incorporate ESG into their investment decisions, driven both by profitability and ethical values, as well as by legislation such as the EU Sustainable Finance Disclosure Regulation.

Many tender opportunities now require the bidder to show compliance with minimum ESG standards before a bid will be considered. This is in addition to the long-standing procurement considerations of value for money and liquidity. It is no longer enough to offer work at a competitive rate. Increasingly, bidders need to offer value alongside evidence of good corporate citizenship.

This is the ‘carrot’ approach. Businesses that are not able to demonstrate good ESG credentials will not be as attractive in the marketplace. Businesses that can have a broader range of appeal and a competitive edge.

Consumers make purchasing decisions based on the values and reputation of a business. It has ever been thus, but in an age where bad news spreads at lightning speed across the internet and social media, the stakes are higher than ever. If a business has a poor environmental record, or a story breaks about exploitation in a supply chain, this does not mean that its products are, objectively, any better or worse. But consumers will react, and sales will almost certainly fall. It is not always labelled as ESG, but that is the basis on which these decisions are made.

A good ESG strategy works to protect a business’s reputation and its standing in the eyes of consumers.

Growing awareness

ESG pervades all aspects of corporate life. The best ESG strategies adopt a holistic approach to values and compliance. Although they have been given a recent rebrand, there is really nothing new about ESG principles – but there is an increasing urgency about applying them, driven by growing global awareness of the fragility of our climate (hence ‘environment’ leading, both literally and metaphorically).

The twin ‘carrot’ and ‘stick’ approach to ESG performance is driving improvements across the board. A considered ESG strategy is increasingly to be thought of as fundamental to doing successful business in the 21st century.

> “There is really nothing new about ESG principles – but there is an increasing urgency about applying them.”

Communities – Sustainable urban centres

- *How can ESG principles help redevelop urban centres?*
- *Can they still support investor landlords' ROI?*
- *What are the challenges to change?*

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Communities – Sustainable urban centres

One of the many societal shifts seen over the last few years has been around consumer behaviour and what is now looking like a permanent altering of how we purchase products and services. How we use the land and property within our urban centres has struggled to keep up with the changes in buying habits, resulting in the now familiar sight of empty units and increasing dereliction in many parts of our towns and centres.

However, as ESG continues up the agenda in boardrooms around the world, a new model of collaboration appears to be emerging in our town and city centres that has social at its core. With property owners less able to rely on big retail brands to fill their centres, the question of what comes next is being answered through the emergence of independent start-up businesses and hubs that offer a more overt link to their communities.

Over the last year, Shoosmiths has been working on a project – Platform: a town centre innovation programme – to explore what more can be done to open up town centre property for a more diverse range of occupiers, while ensuring that investors are sufficiently incentivised and supported to bring them into their schemes. The project has emphasised a number of challenges at the heart of our cities, but also a shared willingness across city centre stakeholders to find solutions that will breathe life back into our cities.

"We need to look outside of the familiar names for the occupier of the future," says Matt Soffair, Research Manager, Retail and Leisure Real Assets at Legal & General Investment Management. "We feel there is a big opportunity and a big demand from consumers for more locally orientated businesses that are plugged into their communities and offer something different."

Social impact

Matt Soffair points to LGIM's Kingland project in Poole, a new curated shopping street, comprising local independents and SMEs that have been given a shop with no rent and no business rates for the first two years. "This is partly a social impact initiative but also a reflection on where we think the market is heading. If you own retail assets, this is the direction of travel. Yes, there is an important ESG angle, and I don't think enough is said about the social value a lot of retail assets have to their communities, however it is also a commercial necessity."

As more schemes based around social impact crop up around the UK – see Bywater Properties' Smithfield Yard scheme in Belfast as another example – a shift in emphasis to a more balanced blend of occupier types than has been seen previously is notable. Fewer empty units mean enhanced aesthetics, greater footfall, social value and, importantly, a financial return for forward thinking property owners. However, such an approach is not without risk, and getting each of the various stakeholders to understand their own aims and the value that can be provided, is merely the starting point.

Shoosmiths is one of five lead partners in the Platform initiative, a town centre property innovation programme that aims to take advantage of the changed post-pandemic landscape as a generational opportunity to redesign how we organise the land and buildings at the heart of our neighbourhoods to bring about positive social change.

The project has brought together individuals and organisations with experience of the retail/commercial property system, from community entrepreneurs and local government to national retailers and institutional investors, to share best practice, promote innovations in property access and ownership, lead the debate on how we move beyond the 'landlord–tenant' relationship and make policy recommendations to government.

Our fellow partners on the project are High Streets Task Force, Power to Change, British Property Federation, New Local and Radix. We have also assembled a working group comprising diverse leaders representing community businesses, local government and investors from across the UK to support the programme.

Evidence of ROI

"There has to be more evidence of the ROI that is made and it has to be provided in language that landlords understand," says Liam Kelly, CEO, Make CIC, a social enterprise that runs workspace hubs in the north west for start-up businesses in the creative sector. "One challenge is that the various parties involved don't all speak the same language. You can all want the same outcome but if you're not communicating then you may not have the opportunity to work together. But there are great examples of investor landlords doing great things. If you can focus on that return on investment and support them to add value, then it can work."

Matt Soffair agrees: "There needs to be evidence of business planning and a model that can support rent payments in the future and the long-term growth of that business, as well as offering something different that fits into the local environment. However, they also need to be able to offer things that are important to other businesses in our schemes, such as seven-days trading and the opening hours of the scheme.

Closer relationships

"Owners need to enter into more conversations with their occupiers to understand what their offering is, and that requires a more adapted partnership approach than has been done in the past to develop closer relationships and support for each other. It is a more intensive model of managing real estate but, in attracting more local and independent businesses, it ultimately benefits the wider scheme and that investment in time and resource becomes worthwhile. It is a shift from being what was a librarian of space to being more of an editor of space."

There is clearly more to do to support diversity in our urban centres, but the opportunity is there to be taken. As Liam Kelly says: "We are seeing more opportunities to influence the conversation moving forward, as better ESG outcomes become demanded or even required [by law]. It's only moving in one direction and socially trading organisations are in a great position to supply more solutions to, for, or in partnership with corporates."

Green finance – Sustainability linked loans

- *How are ESG principles shaping lending?*
- *What is holding back the market?*
- *How do we deal with the unintended consequences?*

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Green finance – Sustainability linked loans

With ESG now a focus for all companies, more questions are being asked by a wide variety of stakeholders including employers, consumers and supply chain partners around the ESG credentials of products, services and investments. The same pressure is coming from employees demanding more from their employers, prompting the realisation that businesses of all types can no longer bury their heads in the sand if they want to avoid financial and reputational damage.

“Individuals are helping to drive the ESG agenda and that is filtering up through organisations who are tackling it from the top down,” says Chris Williams, Head of Project Finance, London at Landesbank Baden-Württemberg (LBBW). “That meeting in the middle is one of the reasons why we are seeing a change in emphasis on ESG.”

Still early days

In the financial services sector, while the ESG agenda is top of the priority list for almost all institutions the actual provision of green and sustainability linked finance can be inconsistent, with both lenders and borrowers coming to terms with the concept of sustainability-linked loans. However, the market is advancing all the time - last year Shoosmiths advised on one of the largest regional sustainability-linked loans and, as Debra Cooper, a partner in Shoosmiths’ banking team who led the deal, says: “12 months on, that deal would look very different now.”

She adds: “Government is encouraging banks to provide green loans but offering little guidance on how to do it, and when you look at the consequences of greenwashing, the market is understandably wary. As a result, we are seeing green loans being driven by the bigger banks in the short term as smaller banks often won’t have the resources to dedicate to it”

LBBW is evidence of this – a mid-sized international bank that takes ESG very seriously, to the extent that it now has three distinct advisory groups – for corporates, for savings banks and for not-for-profits – whose sole focus is ESG. Patrick Schwiertz, Head of Sustainability & ESG at LBBW, says: “The last two years have seen an acceleration in progress with ESG. One example is our updated coal policy that we passed last year and, for instance, now excludes general financing for energy suppliers that build new coal plants. That is a big change from four years ago.”

Shoosmiths advised Lloyds Bank on one of the first sustainability-linked four-bank deals outside of London in 2021, a £280m sustainability-linked development and investment facility to Bruntwood Scitech for the refinance of existing UK based assets, the purchase of Melbourn Science Park and the development of Innovation Birmingham Campus. The consortium comprised Lloyds, NatWest, Santander and HSBC.

The funding will enable further growth and investment in the fast-moving science and technology sectors and will enable Bruntwood Scitech to positively contribute to the wider climate change agenda.

> “Every business along the supply chain has to now get on board with it or risk being left behind.”

“

People who are talking the talk but not walking the walk will get found out.”

Doing the right thing

So, progress is slowly – albeit sporadically – being made by lenders, but is there sufficient demand from borrowers?

“We are seeing some but not massive demand at the moment,” says John Carter, Commercial Director at Aldermore Bank. “For us, it is really about embedding ESG into the daily operations of everyone in our supply chain so that it becomes a self-fulfilling prophecy. It is about doing the right thing and awareness is growing. Collaboration is key here as we can all learn from each other and across the industry and understand what we can do that is authentic to our business.”

One possible reason for the variable take-up by borrowers is that the green finance market is currently based on incentives. Debra Cooper says: “At the moment, typically there is a pricing incentive with green loans – if you can tick certain ESG boxes then you can get a better interest rate. However, as the market gets more mature and established, we will get to the point where, if your assets are not ESG-compliant, then you won’t be able to borrow money against them. So, if you have a large property portfolio where half of your assets are not at the standard required by your ESG-linked loan, you have a decision to make. Either undertake a costly retrofitting programme or go to a smaller bank or a different type of funder. There is a huge risk that asset owners will struggle to find funding for under-performing assets at a price they are used to.”

This view is endorsed by Paul Brocklehurst, Chairman of the Land Promoters and Developers Federation: “Businesses are thinking about ESG in a very narrow focus. It becomes more topical for larger organisations who have greater resource to dedicate to it, shareholder pressure, customer expectations and larger supply chains. If all funding became ESG-linked, we’d have a major problem in this country as many smaller real estate businesses won’t have resource to dedicate to capture and report on ESG-linked KPIs.”

Sheelagh Cooley, a partner in Shoosmiths’ real estate finance team, goes further: “SMEs will find it more challenging to access green finance than the larger, more established operators. It is critical that appropriate support is given to the SME sector to ensure they can access green finance as many such companies will be the owners/occupiers of older buildings where retrofitting will be required and relocation or replacing that building with a new sustainable building will not be an option. It is incumbent upon lenders and larger corporates to ensure that doesn’t happen by sharing their knowledge and expertise – it’s only in that way that the built environment as a whole will be able to achieve its carbon reduction targets.”

Measurement

A key challenge to the advancement of ESG-linked loans is around the measurement of compliance, which at the moment, Debra Cooper says, is "like the wild west, with a real lack of consistency a cross the market and sectors."

Chris Williams agrees: "In terms of measurement of KPIs on ESG-linked loans, it is fair to say it is in the developmental stage. In the renewables space, for example, you can look at the number of gigawatts of energy being produced, the number of homes being powered by green energy and CO2 savings, but there isn't a standard set of KPIs that everyone adheres to and different companies have their own interpretation of what is important – it needs more consistency."

"There is also the issue of who is qualified to do that measurement," says Debra Cooper. "Some banks have assembled green loan compliance teams, but there is a cost attached to that which may get passed on to the borrower, wiping out the original cost saving from the green loan. It also places more responsibility on the banks to resource this and is a much bigger job than the government first envisaged."

However, in order to measure accurately you need accurate data. "Data integrity is a key challenge for financial climate analysis," says Ryan Friel, Operational Risk Manager at LBBW. "Climate related financial data is very much in its infancy and this feeds into measurement methodologies that produce climate change metrics, which are already based on assumptions."

Transparency

For all the challenges and teething troubles of an embryonic market, it is clear that there is little place to hide, with government, industry and consumers increasingly committed to calling out and combatting greenwashing. "People who are talking the talk but not walking the walk will get found out in the coming years because there is a lot more transparency coming into the industry," says Matt Soffair, Research Manager, Retail and Leisure Real Assets at Legal & General Investment Management. "It's non-negotiable now and at the forefront of our clients' minds, and therefore is at the forefront of our minds."

Chris Williams says: "With EU taxonomy making everything more transparent, people can decide where they want to invest their money at shareholder level. So there will naturally be a flight to businesses with ESG credentials and carbon neutral strategies, as we see more requirements come through for reporting of it. Recalling the 10-point plan the government set out in 2020 for a green industrial revolution, investing such a heavy amount of capital into carbon neutral initiatives to hit net zero targets shows that businesses (particularly large companies) along the supply chain will need to do their best to be on board or risk being left behind."

Office investment – ESG quality comes at a cost

- *How are ESG principles shaping the demand for office space?*
- *Are new offices necessarily greener?*
- *Can renovation also meet ESG aspirations?*

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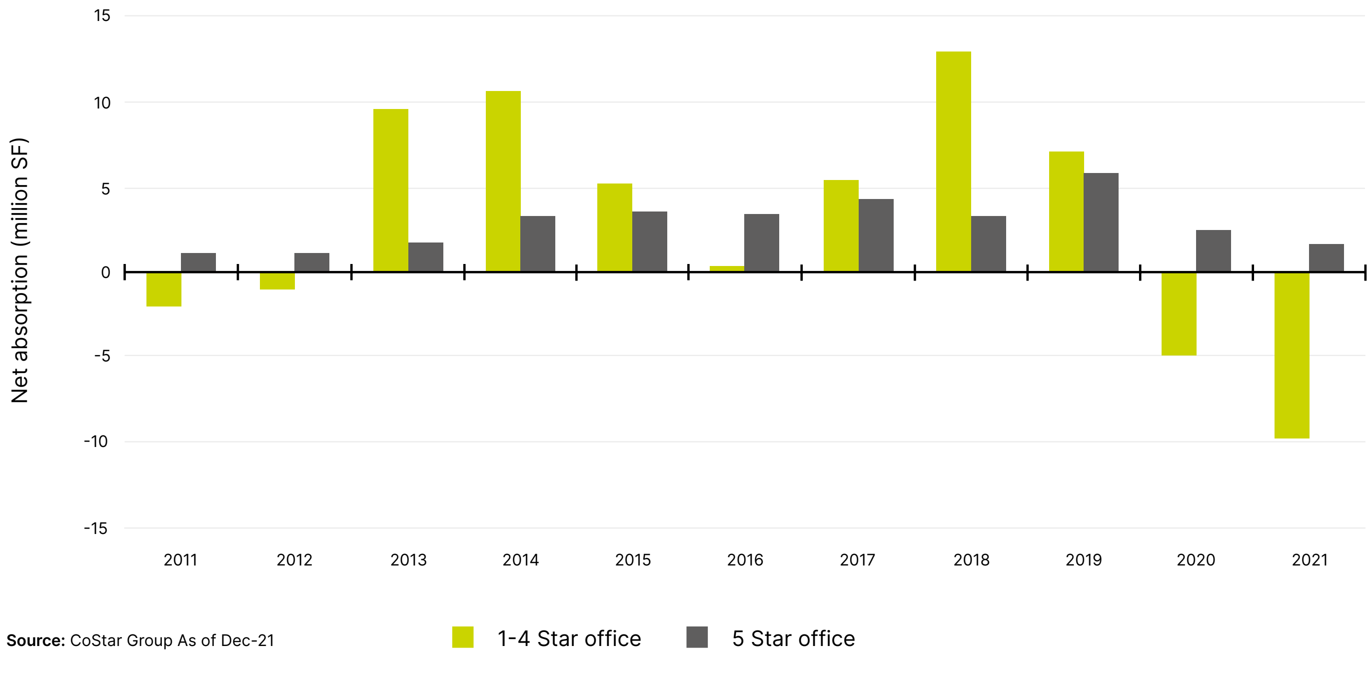
Office investment – ESG quality comes at a cost

Whether it is AstraZeneca moving to a new 37,000 sqft headquarters at King's Cross Central, Google's acquisition of 408,000 sqft of offices at Central St Giles in Paddington or Omnicom's acquisition of the 450,000 sqft Bankside buildings, recent activity suggests the office market is not dead.

While London saw its highest quarter of occupier activity since before the pandemic at the end of 2021, according to Gerald Eve, this trend is certainly not exclusive to the capital. There was NatWest's purchase of 368,319 sqft at 1 Hardman Boulevard in Manchester, the biggest regional office deal of 2021 until Segro broke that record a few hours later with its 958,000 sqft purchase of an office portfolio in Slough.

But there are patterns to discern behind the headlines with this activity primarily being led by a gravitation towards best-in-class space and increased demand for buildings with strong ESG credentials. When looking at activity in the sub-prime office market, where ESG performance is less pronounced, the picture is different.

Flight to quality amid rising importance of ESG



Source: CoStar Group As of Dec-21

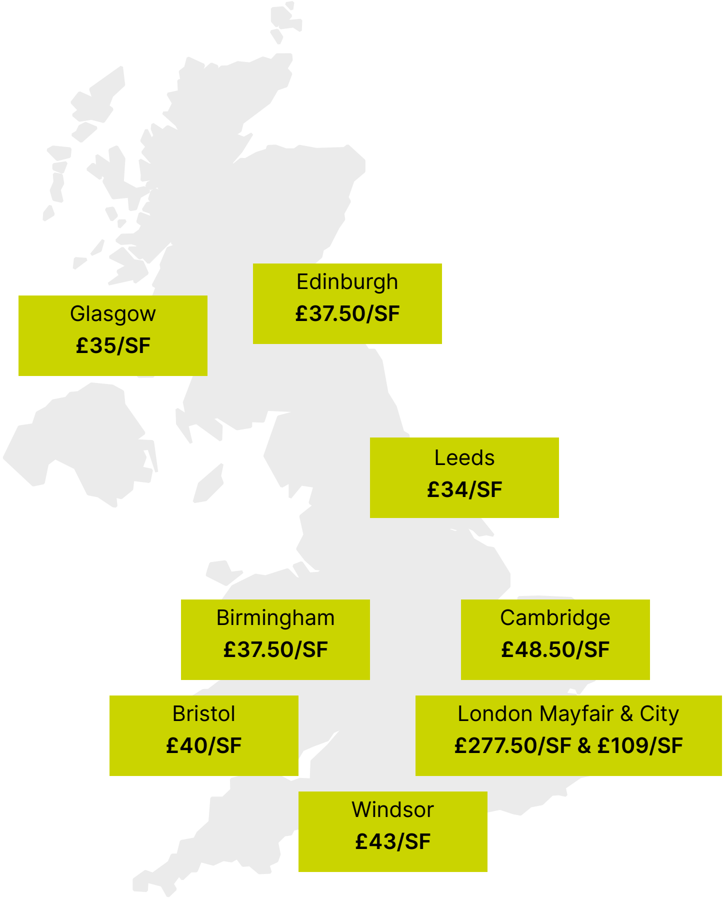
"Our data shows that net absorption in the best-quality, 5-star buildings has been positive throughout the pandemic, with all the demand losses coming in buildings rated 4-star or below," says Mark Stansfield, Head of UK Analytics at CoStar. "Firms are seeking such space to attract staff, welcome clients and meet growing ESG requirements, even if many take less space overall as home working becomes more entrenched."

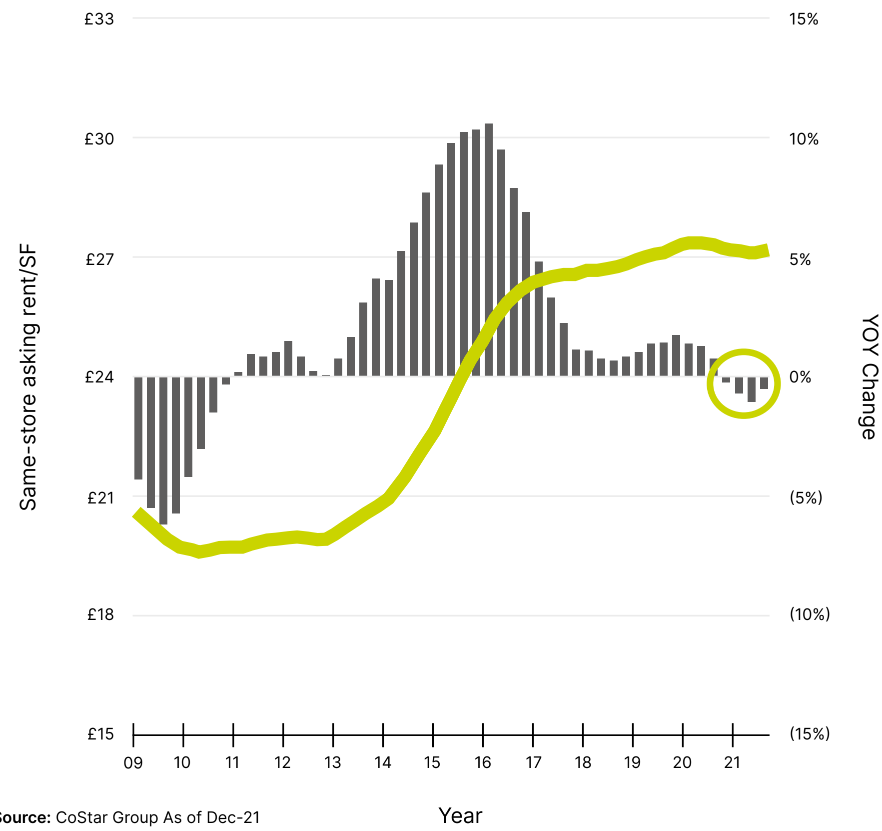
Savills backs up this point in its December 2021 UK Regional Office Investment Market Watch report: "The demand in the market is polarised with prime opportunities which can satisfy ESG criteria and provide medium-long term income being actively targeted."

However, amid this flight to offices with high ESG credentials, one issue continues to be ignored – that of the embodied carbon emitted in producing materials. For example, the production of steel and cement alone makes up between 16-18% of global CO2 emissions annually. What is more, the Royal Institution of Chartered Surveyors estimates that 35% of the lifecycle carbon for a typical office development is emitted before the building is opened. Therefore, while it is correct to say that a new build will be more energy efficient – and demolition will no doubt be the best option for many buildings to make way for new development – it would also be worth challenging whether the difference in energy efficiency on some sites is worth the CO2 cost of production.

> Firms rush to snap up a dwindling pool of high-quality, highly sustainable space."

Prime Rents Grow as Average Rents Fall





Source: CoStar Group As of Dec-21

Regardless, this flight to quality comes at a cost, both in the purchase price but also rent levels. “Strong demand for the very best space has pushed prime rents upwards even as average rents have fallen,” says Mark Stansfield. “Record rents have been recorded in nearly all major markets over the past year or so as firms rush to snap up a dwindling pool of high-quality, highly sustainable space. This comes at a time when average asking rents across the country are falling.”

The Thames Valley, for example, saw four new lettings in 2021 that smashed through the record rents for the region, with InterContinental Hotels Group, InterSystems, Neilson Financial Services and NetApp all taking up BREEAM Excellent office space in Windsor at rents 7-10% up on the previous record set in 2017.

So, with activity at the top end of the market fuelling growth and, to some extent, skewing the overall office picture, a few big questions are left to be answered: what will happen to the sub-prime office stock, what will be the impact on those organisations unable to afford a green premium and what will it all mean for ESG? One thing is for sure – it cannot just be about new builds.

Renovating, upgrading and repurposing of old stock needs to be part of the solution to create a more balanced market. As such, with organisations battling to lure employees back into the office and rebuild their office cultures, it is clear that ESG can act as a powerful driver for growth.

Diversity & inclusion – Measuring the impact

- *How do ESG principles support a more diverse and inclusive workplace?*
- *How far does measurement take us?*
- *Can measurement improve accountable outcomes?*

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Diversity & inclusion – Measuring the impact

In 2022, organisations continue to reckon with diversity, equity, and inclusion issues, and more senior leaders are making a step change in the level of focus their organisations place on making progress. This is happening in a fast-changing work environment and is much needed to ensure organisations fulfil their role both as employers and in society.

One of the most challenging aspects of any strategy, however, is measurement, so we asked some of our external partners to share their thoughts on this question. We have grouped these thoughts into three themes: measurement driving action, continuous progress and accountable outcomes.

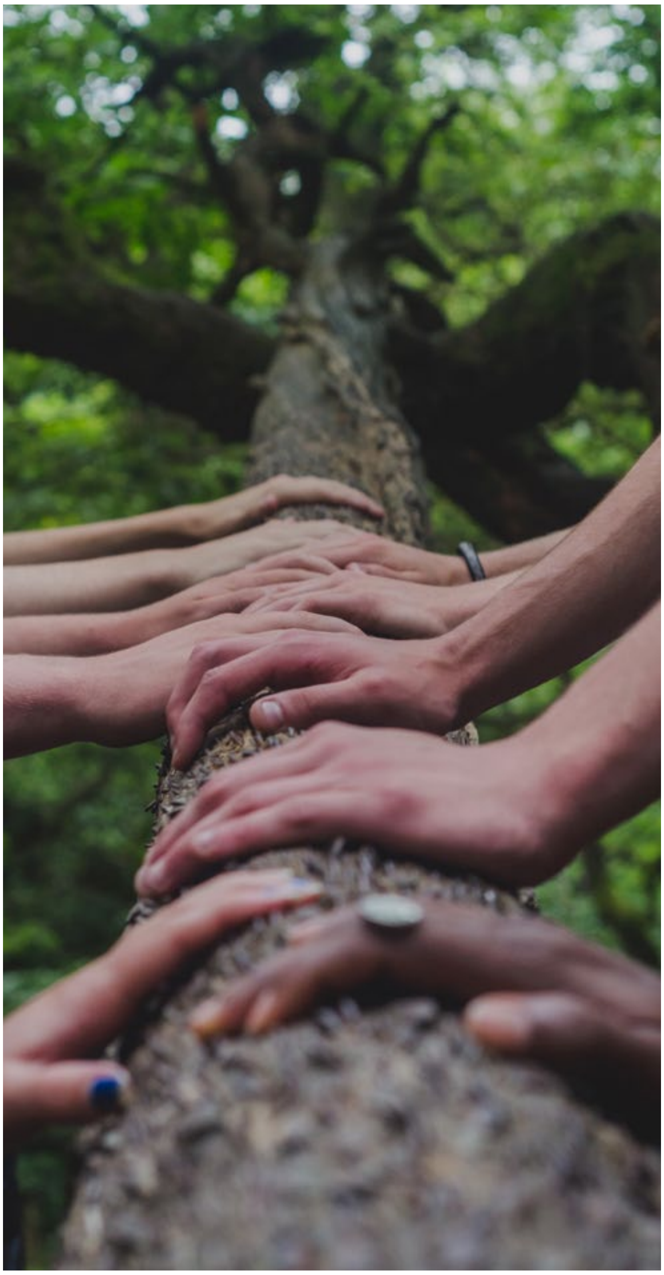
Driving action

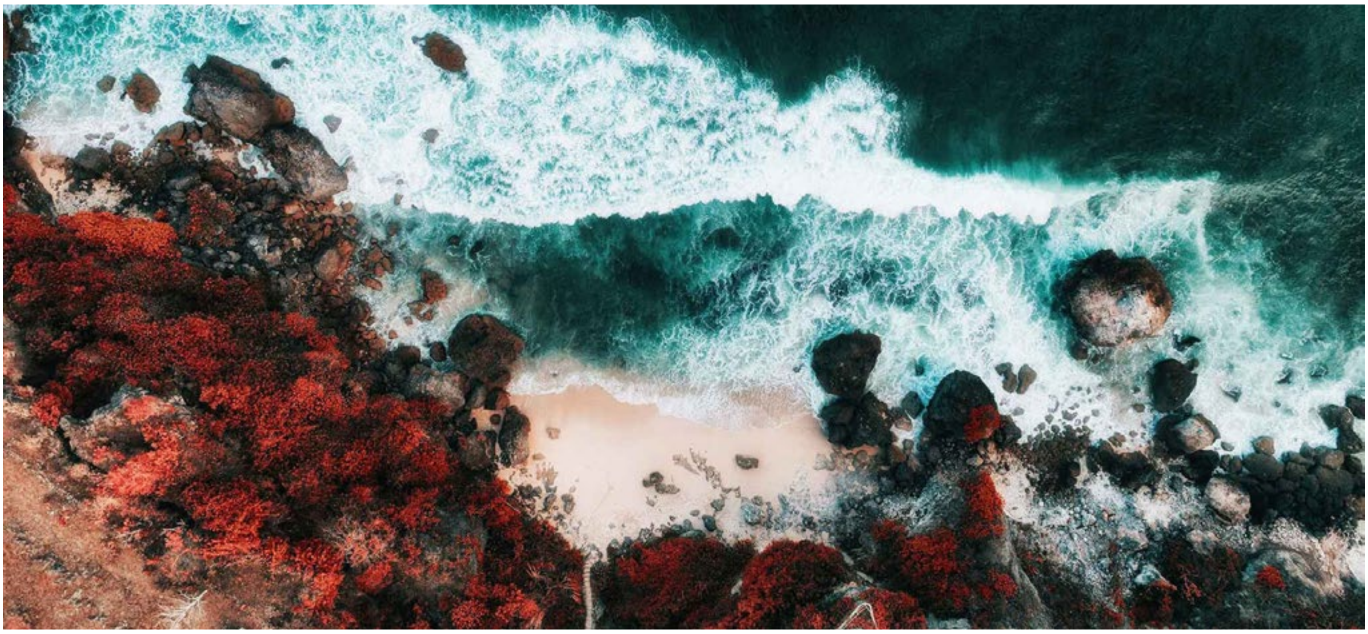
Each year, we engage with an external network and report on our progress across diversity and inclusion and wider ESG issues through the United Nations Global Compact (UNGC). Over 15,000 companies around the world are involved in the UNGC.

"Our objective is diversity, equity, and inclusion [DEI] in the workplace and wider society," says Steve Kenzie, Executive Director at UNGC UK. "Measurement is just a means to that end, which has little value unless it catalyses meaningful action. There needs to be more urgency in addressing DEI issues. Too often we see DEI data revealing poor performance which is then accepted with passive resignation. Action is needed. It's not enough to wait for a few people to retire or for more diverse candidates to apply. This is a critical business issue and a human rights issue."

The Purpose Coalition, a group of business and education leaders working together to have greater impact on society, is led by Rt Hon Justine Greening. Shoosmiths was one of the first businesses to join The Purpose Coalition, following a successful partnership in creating the firm's Social Mobility Action Plan.

"We know that in successful organisations what gets measured, gets done," says Justine Greening. "That's absolutely true for social mobility and organisations that are committed to delivering on their purpose. For the first time, organisations are making real moves towards tracking their socio-economic diversity and measuring progress. We know that employers can be engines for social mobility – and it's time to start tracking progress."





Continuous progress

As well as driving action, measurement can have the most impact when regularly revisited and tracked over time; particularly when benchmarked against others.

“D&I initiatives often stumble at the first hurdle: what does ‘good’ look like,” says Jason Ku, CEO at analytics organisation Pirical. “One thing we see is that by ethnicity, for example, the whole legal industry is becoming more diverse. So, most firms can point to making some sort of progress, without really trying. What then becomes important is comparing rates of change. Is the firm under- or over-performing the market trend? Is that driven by recruitment, attrition or promotion? Getting enough data to benchmark over time – say, five years – can be hard, particularly for regional or specialised firms. A collective of firms, including Shoosmiths, has committed to pooling data to solve this problem.

“In 2022 we expect to see more tools on the market that support people managers to work with real-time data and intervene before it’s too late – for example: which individuals are not getting enough exposure to high-value matters?”

Accountable outcomes

Street League is one of the Shoosmiths Foundation’s grant partners and has been using transparent impact reporting and live data to improve its outcomes and future decision making, and to hold itself accountable.

As part of its continued commitment to tackle inequalities that prevent young people moving into work, Street League uses the government’s racial disparity audit to regularly review its data to monitor outcomes, which includes gender, ethnicity and postcode. It has set a target to reach 50% female participation by 2025-6 (currently at 30%) and regional ethnicity targets are set annually.

It aims to reduce disengagement by 10% each year and ensure its support is for those who need it most, with 75% of young people reporting at two or more personal barriers. It reports its impact on a monthly basis through its online interactive dashboard.

Real estate development – Getting down to zero

- *How are ESG principles shaping lending?*
- *What is holding back the market?*
- *How do we deal with the unintended consequences?*

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Real estate development - Getting down to zero

Climate change has been put at the top of the agenda for many businesses with two recent events in particular fixing the focus on action. First the publishing of the Sixth International Panel of Climate Change (IPCC) Report in August 2021, which in summary declared:

- **Climate change is a fact of life**
- **It is a crisis - a code red for humanity**
- **It is caused by fossil fuels**

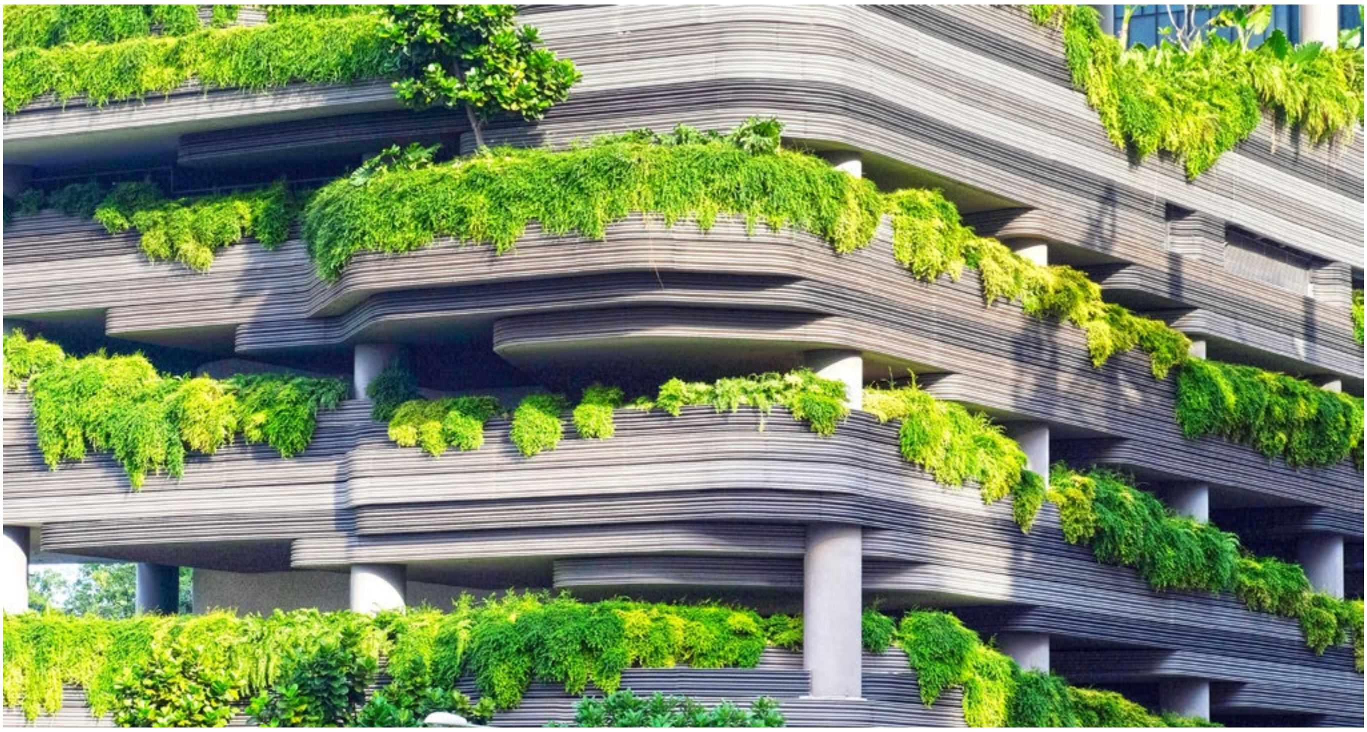
> "The sector still lags behind other industries in respect of material and component parts being dismantlable and reusable."

The IPCC is famously conservative with its findings due to the requirement of needing them to be agreed by 195 countries. Yet the report boldly declared: "Humanity is unequivocally responsible for climate change". This is as close as we get to scientists screaming at the top of their lungs from tall buildings.

The second event was COP26 and the publishing of the Glasgow Climate Pact in November 2021. The need for action was quite clear with Para 17 of the Pact following the IPCC Report recognising that "rapid, deep and sustained reductions" were needed in global greenhouse emissions to keep the 1.5oC target in reach. The Pact also highlighted a move to measurable mitigation measures rather than vague targets. It may also be surprising to note that this was the first ever mention of fossil fuels in the text of a COP agreement.

The impact of the sustainability zeitgeist is already evident in the rising importance given to ESG considerations, with many investors and lenders now treating ESG risk as investment risk. Indeed, many businesses are now beginning to report performance on an ESG metric and on this basis the "E" is the immediate existential threat. To put it into context, to get to the 1.5oC warming scenario of the Paris Agreement, we need to reduce global emissions 6% per year - the equivalent to a Covid-type disruption event a year for the next couple of decades.

The buildings and infrastructure sector is still one of the largest carbon emitters, directly responsible for 25% of the carbon footprint and rising to 42% when surface transport is added. The built environment has some very challenging issues to address.



The way forward

With the UK having now legislated for net zero carbon by 2030, as an economy there has been a definite shift in attitudes across the whole value chain, from agents and valuers to architects and developers. Terms such as 'climate change mitigation', 'nature and biodiversity', and 'resource circularity' have become more prominent in the concepts driving real estate development as the sector moves to actioning the ambition of a net zero built environment.

Considering that many developments can take up to eight years from inception to completion, the built environment as an industry cannot be planning steps over the next eight years to halve emissions by 2030. Rather it needs to have a joined up and progressive approach to how it develops now. The UK Green Building Council has recently launched its Net Zero Whole Life Carbon Roadmap – this is a positive step as it aims to establish pathways to decarbonisation to enable stakeholders to make informed market decisions rather than second guessing. This joined up approach is essential.

Along with the shift in industry attitudes, there also needs to be a regulatory and policy shift with flexibility and adaptability being promoted as core attributes of the built environment. For instance, we need to see more integration of a circular economy as part of real estate development. The sector still lags behind other industries in respect of material and component parts being dismantlable and reusable.

In terms of regulation, we need to see less strict uses and zoning regulation, which hinders the adaptability of the built environment. The built environment needs to enable and facilitate supply chains and businesses to decarbonise, not curtail or hinder them.

Innovation also needs encouragement, and perhaps the first step should be putting innovation in respect of sustainability on an equal footing by changing the procurement rules and giving innovation a more prominent consideration in assessing and awarding contracts, rather than cost analysis.

It is certain that the built environment has an integral role to play in the low carbon transition.

The green shoots of progress

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The green shoots of progress

Some bite-size observations on the perceived progress being made around ESG.

A couple of years ago, the focus was on the margin, but increasingly borrowers want to do the right thing so there is bottom-up demand from borrowers for ESG-linked loans. And if the return is there, then everyone wins."

Debra Cooper, Banking Partner – Shoosmiths

I feel that 2022 will be the year in which we see a lot more action on all of the E, S and G.

Matt Soffair, Research Manager, Retail and Leisure Real Assets – LGIM

A considered ESG strategy is increasingly to be thought of as fundamental to doing successful business in the 21st century."

Joanne Sear, Principal Associate, Environmental Regulatory – Shoosmiths

For the first time, organisations are making real moves towards tracking their socio-economic diversity and measuring progress."

Rt Hon Justine Greening

In 2022 we expect to see more tools on the market that support people managers to work with real-time data and intervene before it's too late."

Jason Ku, CEO – Pirical

Potential barriers to progress

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Potential barriers to progress

Some bite-size observations on the ongoing challenges we face around ESG.

“

We need to remove some of the barriers that are in place for smaller occupiers to make the process of taking space as friction-free as possible. No one wants empty shops, so we need to make the process of accessing space easier and quicker.”

Matt Soffair, Research Manager, Retail and Leisure Real Assets – LGIM

“

There is still no generally accepted definition of what is (and isn’t) included in the term ‘ESG’. For anyone starting out on developing an ESG strategy, that makes it difficult to know what aspects of their business and its impacts they need to be looking at.”

Angus Evers, Partner, Environmental Regulatory – Shoosmiths

“

One challenge is that the various parties involved don’t all speak the same language. You can all want the same outcome but if you’re not communicating then you may not have the opportunity to work together.”

Liam Kelly, CEO – Make CIC

“

There needs to be more urgency in addressing DEI issues. Too often we see DEI data revealing poor performance which is then accepted with passive resignation. Action is needed. It’s not enough to wait for a few people to retire or for more diverse candidates to apply.”

Steve Kenzie, Executive Director – UN Global Compact Network UK

“

In the UK, there is a strong focus on the E, but in order to make progress on the E, you need to ensure you are delivering on the G which is why strong culture and leadership are imperative.”

Ryan Friel, Operational Risk Manager – Landesbank Baden-Württemberg

What is Shoosmiths up to on ESG?

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What is Shoosmiths up to on ESG?

- Click here to learn more about the Shoosmiths Foundation.
- Click here to learn more about Shoosmiths' approach to diversity and inclusion.
- Click here to learn more about Shoosmiths' ESG priorities and the progress it is making.
- Click here to read our ESG blog, SHOUTback
- Click here to read our annual ESG report and 2022 United Nations Global Compact report.
- Click here to read about Shoosmiths signing the Green Pledge, a global initiative to minimise the environmental impact of arbitration.

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