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Urban Land Institute

C Change check-in: demystifying transition risks and valuation

Moderator

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C Change check-in: demystifying transition risks and valuation

Presenter

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C is for come on board and join the movement.

Lisette van Doorn | C Change update

“We are on a highway to climate hell with our foot still on the accelerator.”

UN Secretary General, António Guterres, COP27

39%

The built environment is responsible for the largest share of global carbon emissions. We have a responsibility to address this challenge together as an industry.

Real change with C Change

Practical solutions and collective action for industry transformation

- ULI-led multi-year programme to mobilise the industry to speed up and scale up decarbonisation in Europe.
- Accelerating solutions that will transform our industry and protect our planet.
- A movement to connect the brightest minds from across the value chain.
- A focus on systems interventions to enable industry-level change.

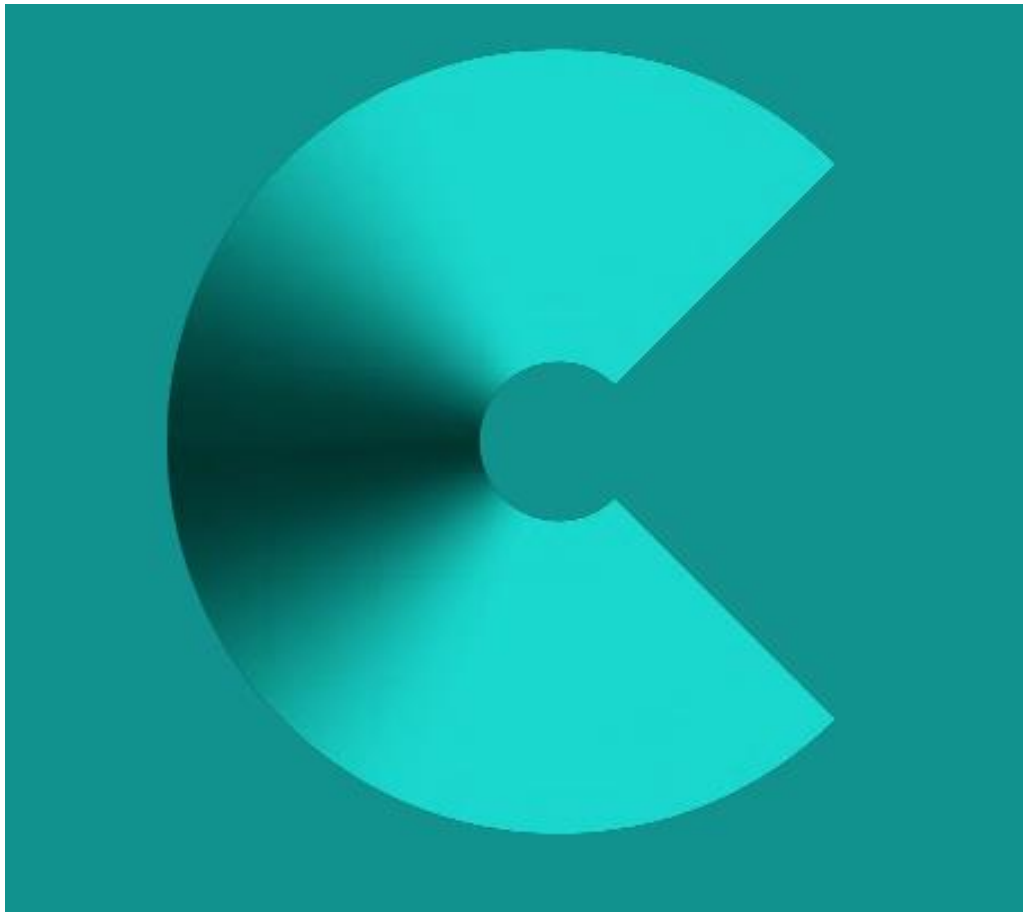
Interventions points identified for action

Assessing transition risks intervention

Unlocking the valuation issue is critical

Major barrier to a fast and effective transition

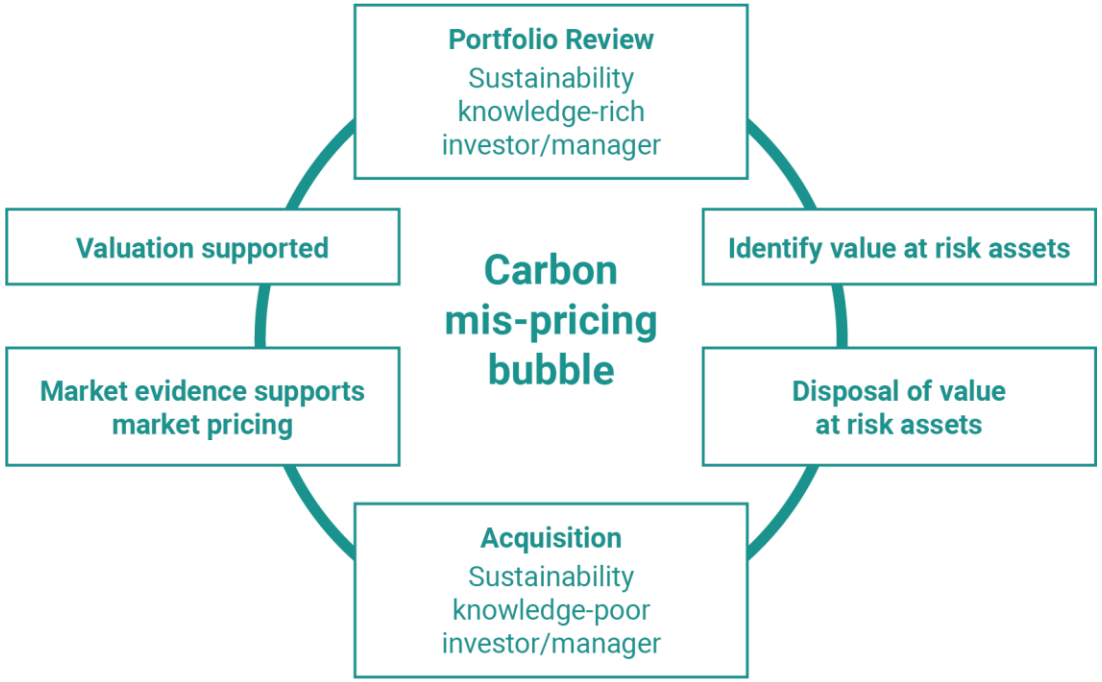
- Current property valuations are holding back the industry's progress towards decarbonisation.
- Climate transition risks are not factored into valuations:
  - no regulation to set deadlines for net zero
  - Valuers need evidence of the impact of transition risk
- Decarbonisation of physical assets is a societal issue, as well as a technical building issue.
- This is not just about **whether** we act but **how** we act.



Acknowledging the carbon bubble

Bubble of carbon mis-pricing from valuation of low energy performing assets

- Pricing bubble propelled by knowledge gap in market
  - Investors well informed on transitions risks have better knowledge to inform buying/selling activity often with less sophisticated investors
  - Where both sides have knowledge, this is reflected in pricing but valuers cannot attribute to net zero pathways
- Overall industry decarbonisation efforts are being slowed or hampered
- Bubble requires deflating to avoid damaging huge impact on values



Danger of inequality in cities worsening

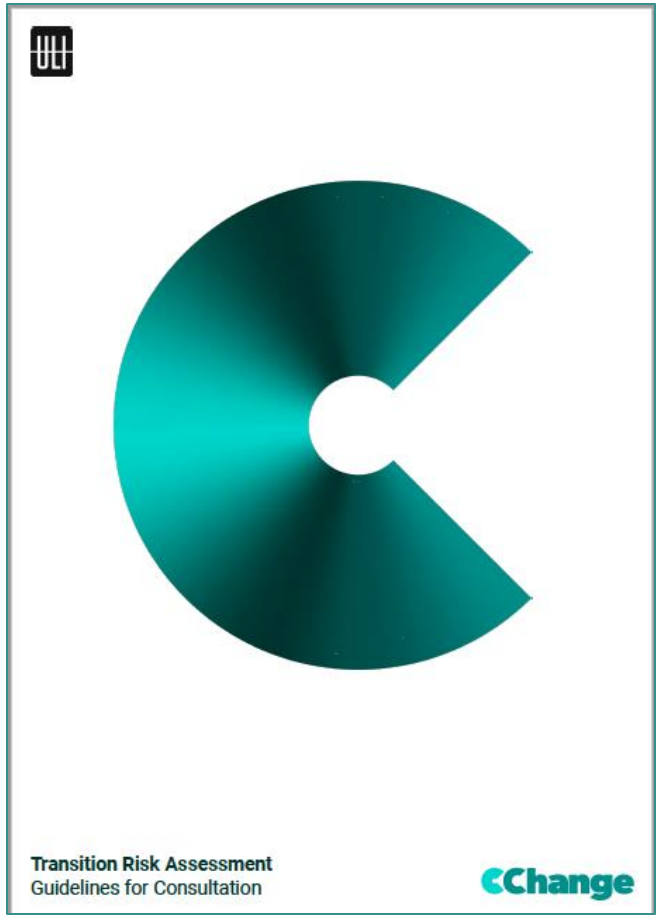
Possibility of a two-tier market between assets in high and lower-value locations

- Higher value locations benefit from more viable business case of retrofitting:
  - Lower ratio of transition costs to value
  - Higher concentration of leading occupiers
  - Expectation of “green” rental premium
- Valuation process reinforces viability for higher value locations.
- Less viability in lower value locations, resulting in less investment and more stranded assets.
- Ensure all assets are transformed for a just transition.

Solution comes through a common approach

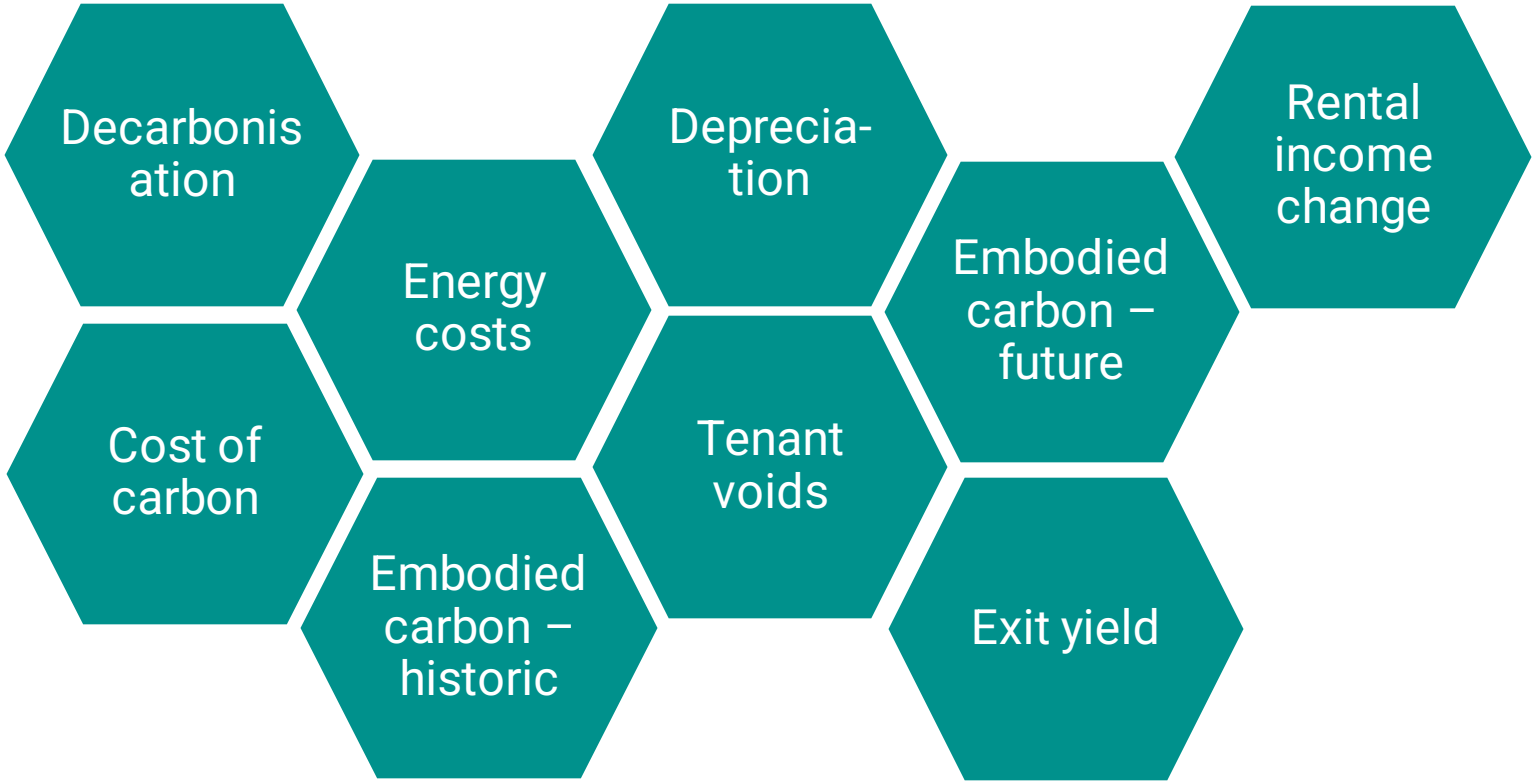
Guidelines out for consultation until Q1 2023

- Consultation guidelines for a common methodology to assess and disclose transition risks.
- Identifies 14 transition risks, of which nine can be quantified.
- Proposes disclosure sheets with data points for transparent information transfer.
- Requires a mindset change to remove transition risks as a competitive part transactions.



Nine risks can be quantified and assessed

A standardised method for assessing and integrating transition risks in a DCF



Example: energy costs

Guidelines set out principle and proposed treatment

Proposed principle: An accurate estimation of inflation adjusted energy costs must be included in the discounted cash flow, before and after all acts of decarbonisation events, for the full duration of the holding period.

Proposed treatment now:

Accurate estimates of

- the potential additional costs (eg rising energy prices)
- the potential cost reduction (eg reduced energy usage as a result of decarbonisation activities),
- new potential income opportunities (e.g., surplus energy sold to the grid) are clearly understood.

Proposed treatment future:

- Estimate the rise in the cost of energy sources over the time frame of the discounted cash flow with informed decisions on the appropriate rate of inflation and include that as part of the risk premium calculation in the nominal discount rate.

Example: energy costs

Guidelines set out principle and proposed treatment

Proposed placement in the discounted cashflow

TRANSITION RISK ADJUSTED MODULE EXCERPT	Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
OPERATING EXPENSES										
Utilities	**Last reporting year total cost**	**Yr 1 + inflation adjustment**	**Yr 2 + inflation adjustment**	**Yr 3 + inflation adjustment**	**Total cost reduction + inflation adjustment**	**Yr 5 + inflation adjustment**	**Yr 6 + inflation adjustment**	**Total cost reduction + inflation adjustment**	**Yr 8 + inflation adjustment**	**Yr 9 + inflation adjustment**
Grid Electricity	Last reporting year energy type cost	Yr 1 + inflation adjustment	Yr 2 + inflation adjustment	Yr 3 + inflation adjustment	Cost reduction event as a direct result of act of decarbonisation + inflation adjustment	Yr 5 + inflation adjustment	Yr 6 + inflation adjustment	Yr 7 + inflation adjustment	Yr 8 + inflation adjustment	Yr 9 + inflation adjustment
Natural Gas	Last reporting year energy type cost	Yr 1 + inflation adjustment	Yr 2 + inflation adjustment	Yr 3 + inflation adjustment	Yr 1 + inflation adjustment	Yr 5 + inflation adjustment	Yr 6 + inflation adjustment	Cost reduction as a direct result of act of decarbonisation + inflation adjustment	Yr 8 + inflation adjustment	Yr 9 + inflation adjustment
Fuel Oil	Last reporting year energy type cost	Yr 1 + inflation adjustment	Yr 2 + inflation adjustment	Yr 3 + inflation adjustment	Cost reduction as a direct result of act of decarbonisation + inflation adjustment	Yr 5 + inflation adjustment	Yr 6 + inflation adjustment	Yr 7 + inflation adjustment	Yr 8 + inflation adjustment	Yr 9 + inflation adjustment
District Heating: steam	Last reporting year energy type cost	Yr 1 + inflation adjustment	Yr 2 + inflation adjustment	Yr 3 + inflation adjustment	Yr 4 + inflation adjustment	Yr 5 + inflation adjustment	Yr 6 + inflation adjustment	Yr 7 + inflation adjustment	Yr 8 + inflation adjustment	Yr 9 + inflation adjustment
District Cooling: chilled water	Last reporting year energy type cost	Yr 1 + inflation adjustment	Yr 2 + inflation adjustment	Yr 3 + inflation adjustment	Yr 4 + inflation adjustment	Yr 5 + inflation adjustment	Yr 6 + inflation adjustment	Yr 7 + inflation adjustment	Yr 8 + inflation adjustment	Yr 9 + inflation adjustment
Other energy (renewable)	Last reporting year energy type cost	Yr 1 + inflation adjustment	Yr 2 + inflation adjustment	Yr 3 + inflation adjustment	Yr 4 + inflation adjustment	Yr 5 + inflation adjustment	Yr 6 + inflation adjustment	Yr 7 + inflation adjustment	Yr 8 + inflation adjustment	Yr 9 + inflation adjustment

Benefits bring faster solution and evidence

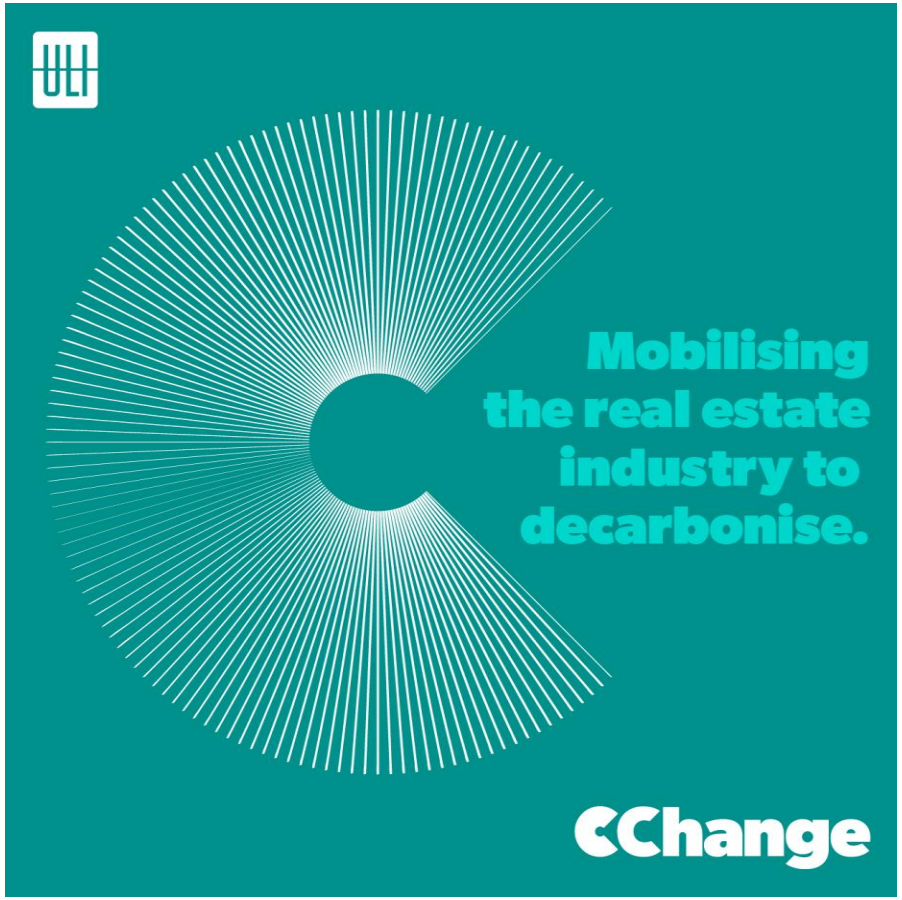
Supports a more effective and fairer transition

- Closes the information gap to support all owners to tackle decarbonisation of assets.
- Helps build business case for greater number of assets
- Creates conditions for a faster transition:
  - A collaborative non-competitive approach
  - Speeds up industry education and expertise.
- Provides evidence base for valuers to factor in transition risks into valuations.
- Offers new evidence as to the benefits of transition such as lower occupational costs, lower voids and potential new incomes streams from renewable energy.

Next steps

Please contribute your views

- Encourage wide industry feedback for the guidelines.
- Programme of engagement including webinars, case studies and interactive events.
- Begin development of Preserve, a smart tool to support industry adoption.
- Explore other areas that would encourage adoption such as data sharing and carbon pricing



Interlinked work scales up adoption

Year two sees more depth and breadth to successful practical approach

Assessing transition risks	Tenant/landlord alignment	Co-ordinated Investment voice	City-scale transition solutions
• Guidelines consultation • Preserve tool • Carbon pricing • Data sharing • Case studies	• Community of practice	• Building key industry advocacy	• Berlin TAP • Advisory panel

Continuation and deepening of year one work

New for year two

Q+A

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Thank you

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for attending the webinar.

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