

Is Your Portfolio Ready For The Next Big Disruption – Climate Change?

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If the events of 2020 have taught us anything, it may be this: prepare for the unexpected. Still unfolding, the COVID-19 pandemic is the black swan event that many investors contemplated, but perhaps couldn't imagine happening – until this year. Now that we've seen the staggering impact one crisis can make on the world, it's only natural to wonder, 'what's next?' This question leads us to arguably one of the most substantial challenges facing real estate, but this time, we've had decades of notice to prepare.

For many commercial property investors, that next major risk is clear. Climate risk has long been top of mind for asset managers concerned about the long-term value of their portfolios. While it may have taken a back seat in 2020 out of necessity, climate resilience remains a clear and present need for institutional investors.

Over the last few years, forward-looking real estate investment managers have increasingly sought to improve energy efficiency and reduce carbon emissions in their portfolios. But mitigating climate change is only

half the equation. Investors must also consider how their managers will respond to the intensifying impact of climate change – from extreme weather and wildfires to rising sea levels – and the enormous strains that these events will place on our cities' infrastructure.

As we begin to understand the likely impacts of our warming planet, it's becoming clear that adaptation planning is needed to protect asset value. These issues can no longer be postponed; asset managers need to consider these risks today to protect their portfolios.

- *Why we can't wait for the next generation to tackle climate change*

Just over two years ago, a 'ninja storm' took the city of Toronto, ON, by surprise as a sudden torrent of rain flooded streets, homes, and commercial buildings in under three hours. The flash flood shut the city down for days as residents waited for flood waters to recede, municipal workers repaired damaged infrastructure, and building owners pumped sewage water out of subfloors and fixed broken systems. According to the Insurance Bureau of Canada (IBC), the violent storm caused \$80 million in insured damage through private claims alone.

Sadly, the flood in August 2018 – offi-

cially classified as a 100-year storm – was not an anomaly. It was, according to the IBC, the sixth 100-year event in the greater Toronto area in the past two decades. And Toronto is not the only city to face increasingly adverse effects of climate change.

As the climate warms, we are seeing more intense impacts throughout the world.

In 2020 to date, brush fires have burned no less than 13.6 million acres in Australia, Hurricane Laura wreaked devastation across Louisiana, wildfires ravaged the state of California, and a hurricane-like storm cut power to tens of thousands of people across the midwestern United States – and that's just a sampling.

For commercial building owners, the prospect of more frequent, more intense weather events can present a major risk. It's not just direct monetary damage, either. Sophisticated tenants want to know that their landlord has sound emergency preparedness measures in place, so a proactive approach is key to attracting and retaining building occupants.

If asset managers don't find ways to mitigate the risks, then assets and their occupants may suffer over time, whether it's due to direct, physical destruction, business interrup-



tion, or market damage.

- **Unlocking the value of climate risk intelligence**

As climate change begins to impact our world in very measurable ways, real estate asset managers can help preserve the long-term value of their assets by taking concrete actions to safeguard properties. Knowing where to start begins with understanding the specific climate risks each building faces. Armed with that insight, smarter decisions can be made about where to invest, how to strengthen new developments and how to operate buildings safely.

- **Make smarter investment decisions**

A decade ago, real estate investment managers bought properties in locations where they expected assets to perform well based on economic and demographic trends. Now, it's also critical to think about how a building is equipped to weather the storms of today and adapt to the changing climate of tomorrow. At BentallGreenOak, we have the ability to assess the climate risk profile of assets we consider for acquisition. This analysis can help inform potential impacts to value and any required mitigation planning.

- **Develop more resilient buildings**

Modern construction techniques enable the building of more resilient structures to withstand the forces of hurricanes, earthquakes, floods, and other natural disasters. It costs more to retrofit properties later, so it's important to address all climate risks in new construction. And when considering sites for development, developers must evaluate the resilience of the city infrastructure that the building will depend upon. For example: is there enough sewage capacity in areas prone to flooding?

- **Reduce risks in building operations**

Most of our cities were erected in an era when climate change risks were not yet understood. For existing assets, it's critical to understand the specific climate risks faced by each building. Experience with evaluating and understanding risk has led us to develop a proprietary climate resilience tool that combines industry research, on-the-ground surveying, predictive climate modelling, and adaptive algorithms to deliver tailor-made climate change plans for each asset.

Based on survey responses from building operators and a database of more than 420 resiliency practices, the tool's algorithms

generate a unique top-10 list of actions for each asset. These bespoke adaptation plans take the guesswork out of climate resilience planning, so asset and operations managers know the top strategies they should plan and budget for, whether it's procuring emergency supplies or investing in backup power generation.

- **Keys to effective climate resilience strategies**

The actions we take today can lay the foundation for resilient portfolios that generate value for generations to come. Tackling an issue as big as climate change isn't easy; it requires time, engagement, and money to make an impact. The five keys to an effective climate resilience strategy are as follows:

- ✓ Understand the unique risks facing each asset: Preparedness starts with understanding a building's risks. At BentallGreenOak, we collect data that assesses risk at the property level. To date, we've developed plans for 413 properties across our North American portfolio, providing timely insight for asset managers responsible for the long-term performance of the properties.
- ✓ Budget and plan for changes: Once you understand the risks facing each asset, you can develop a plan to preserve value and budget for property improvements. Climate adaptation strategies may have an upfront cost, but they create long-term value and help avoid costly repairs and renovations down the line.
- ✓ Create a multi-disciplinary team: It takes a co-ordinated effort to develop and execute climate resilience strategies. A comprehensive approach should involve people from portfolio management, asset management, and operations teams – all working together towards the common goal of protecting long-term value.
- ✓ Create structures for accountability: Since the risks of climate change may sometimes appear to be intangible or far into the future, it's important to create accountability structures to ensure teams address the long-term risks today. Our approach is to tie climate resilience to the annual goals and objectives of our Canadian asset managers.

- ✓ Prioritize governance: Rating agencies and investors alike are increasingly scrutinizing environmental, social, and governance (ESG) factors. As a real estate asset manager, it's more common today to receive due diligence questionnaires to assess our climate resilience strategies. As the need for quality data intensifies, it's important to have strong governance measures to ensure an accurate view of climate risks, strategies, and results at both the asset and portfolio level.

- **Can asset managers rise to the challenges of climate change?**

An asset manager's job has always required a forward-looking approach and a willingness to put in the hard work to create long-term value. It's critical to be vigilant about the changes happening in the world – whether driven by economic conditions, demographic trends, or other forces. As we look ahead, it's clear that climate change will be one of those driving forces.

A robust approach to climate resilience requires streamlined co-ordination between asset management, operations teams, and the real estate industry in general. But the challenges ahead are too big for any one firm to tackle in isolation. By coming together as an industry to share best practices and commit to a common goal, we can develop stronger adaptation strategies that protect not just the value of the assets we manage, but also the people inside them, surrounding communities, and the world we want for the generations to follow. **BPM**



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