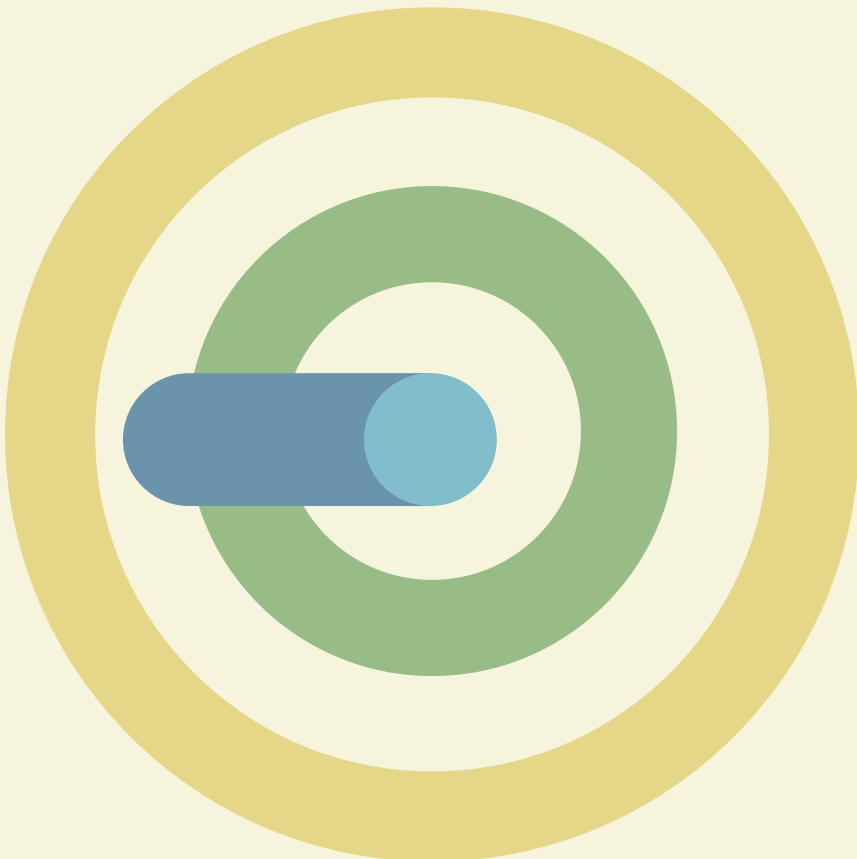
# TARGETED INVESTMENT



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# Sustainable investing now emphasizes precise energy and carbon performance metrics. This shift requires selecting the right metrics and integrating them into the investment process to effectively promote sustainability and boost returns.

Sustainable investing is becoming more precise. Investors are moving beyond simple net-zero goals or GRESB scores, recognizing that these may not always reflect actual energy and carbon performance. The industry now understands that net-zero carbon encompasses both operational and embodied carbon, with operational carbon further divided into site energy use and energy production/transmission factors.

This shift has led to more specific sustainability goals and metrics. Investors now consider whether they want to invest in already green assets or transform brown ones, and whether they prioritize greenhouse gas (GHG) emissions or building-level efficiency. The choice of primary sustainability metric significantly impacts tactics and effectiveness. Importantly, metrics and targets must align with overall investment strategies to be both achievable and profitable.

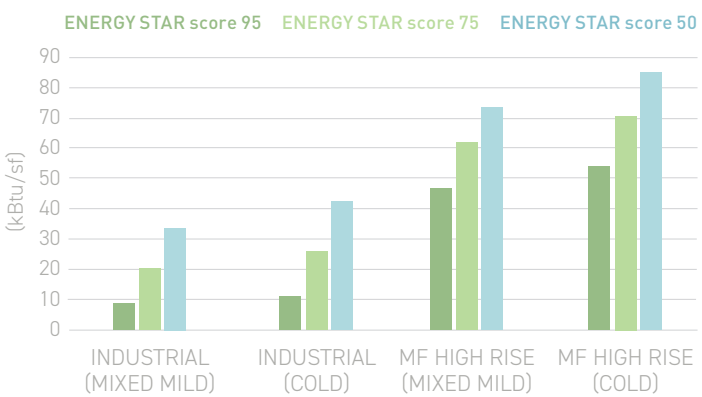
## KEY LEVERS: BUILDING ENERGY USE AND GRID ENERGY SOURCES

The GHG emissions impact of operational real estate can be broken down into (1) energy use and (2) energy sources.

*Building Energy Use*

Ranked in descending order of impact on energy use in real estate - property type comes first, followed by building efficiency and then climate zone.

## EXHIBIT 1: ENERGY USE INTENSITY (EUI) BY PROPERTY TYPE, EFFICIENCY PERFORMANCE, AND CLIMATE ZONE




Source: Urban Land Institute, Technical Site EUI Reference for ESPM Score Derivations (2024)

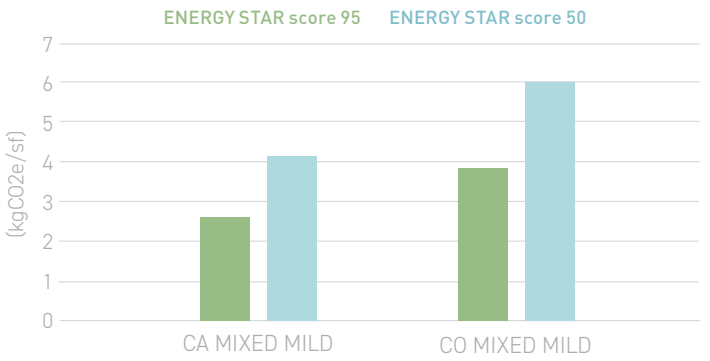
- **Property type** is the most important single determinant of a property's total energy use. For example, low energy intensity property types such as non-refrigerated warehouses may use around 50% of the energy of high intensity property types such as high-rise multifamily. Property type also impacts investors' ability to obtain data and implement improvements. A forward-looking sustainability strategy could prioritize the property types with greater control and ability to electrify—such as low-rise office and multifamily—over more challenging property types, such as high-rise office and multifamily, hotels, shopping centers, and life science.
- **Building energy efficiency** is the second most impactful factor on energy use. The best multifamily buildings uses 15-35% less than the median building, and the best warehouse building uses 40-75% less than the median building. Therefore, selecting efficient assets or increasing the efficiency of assets can significantly reduce overall energy use and GHG emissions.
- **Climate zone** is also a driver of overall energy use. For example, the median industrial building in mixed mild versus cold climates differs by about 25%, and the median multifamily building differs by 15%. Climate zone also has an impact on the ability for properties to electrify, as gas heating is used more in colder climates, where the technical and economic feasibility for heat pumps is also more challenging.

*Grid Energy Sources*

Differences in building-level energy efficiency are multiplied by transmission losses and grid energy mix in determining variation in GHG emissions. Utility regulation and supply have always been under state—rather than federal—control. There are twenty-two main grid regions in the US with different power generation sources, with variations down to the local utility even within regions.[1]

Energy sources and building energy efficiency are almost equally powerful levers influencing GHG emissions. The same building on a relatively clean grid such as California, versus a dirty grid such as Colorado, has a difference in GHG performance of about 45%.

## EXHIBIT 2: HIGH RISE MF GHGI IN CLEAN VS DIRTY GRID




Source: Urban Land Institute, Technical Site EUI Reference for ESPM Score Derivations (2024).

There are 22 main grid regions in the US with different power generation sources, with variations down to the local utility even within regions.

## WHAT SHOULD INVESTORS PRIORITIZE: BUILDINGS OR THE GRID?

It is not possible for a building to get all the way to net zero without addressing energy supply — buildings will always require energy to operate. But it is possible for a building to get to net-zero only through electrification and supply, without addressing efficiency.

The best sustainability strategy should depend on an investor's goals. At a high level, they should seek to articulate their objectives in two main areas:

- **Key Metric:** either directly contribute to climate change mitigation by targeting GHG emissions, or prioritize ensuring that the property uses resources energy efficiently by targeting site EUI, defined as the amount of energy used per square foot per year (which is one of the main factors in reducing GHG emissions)
- **Type of Strategy:** Either purchase and hold buildings that are already high performers or drive reduction over time through "brown to green" efficiency improvements.

## EXHIBIT 3: OPTIONS FOR SUSTAINABILITY STRATEGIES

| PRIORITY | HIGH PERFORMANCE | RELATIVE CHANGE |
|---|---|---|
| GHG EMISSIONS | · Minimize GHG exposure and ultimately reach net-zero carbon<br>· Achieve potential premium associated with all-electric buildings<br>· Manage grid-related risk | · Achieve significant reductions in GHG emissions<br>· Drive returns through potential increased marketability from electrification<br>· Generate revenue through on-site solar |
| ENERGY USE | · Own highly efficient buildings<br>· Minimize exposure to energy cost changes, energy codes, and building performance standards<br>· Achieve potential premium associated with the most efficient buildings (i.e. rent and OPEX) | · Achieve significant reductions in energy use<br>· Reduce exposure to energy cost changes, energy codes and building performance standards<br>· Drive returns through decreasing OPEX and increasing marketability |

Selecting GHG emissions as the primary metric enables a pure focus on carbon-science based Net Zero Carbon (NZC) goals and the macro change towards a low carbon economy. A focus on GHG and electricity grids also helps create market signals for green power generation and electrification of buildings. This means that areas where utilities are not acting strategically to clean up their generation and distribution may see less institutional investment over time.

Nevertheless, energy efficiency remains the primary focus for many US real estate owners and investors. EUI has the greatest alignment with fiduciary and financial goals. Investing in efficient equipment and operations can decrease costs, future proof the building, and make it more marketable to tenants and investors. In addition, whether a building is a relatively high or low energy user can indicate its relative risk exposure to energy price changes and local regulations (e.g., Building Performance Standards).

Energy supply is outside the scope of levers that can generate returns or protect against risk at the property. In fact, paying a premium for green power can be dilutive to returns. Moreover, building owners cannot directly control the efficiency of the electric grid, and recent presidential administrations have taken drastically different stances on energy policy, leading to diverging projections regarding the future energy supply and its carbon intensity.

Looking at total GHG emissions ties to NZC but is agnostic to how that performance is achieved. In other words, an efficient building on a dirty grid and an inefficient building on a clean grid could have the same GHG performance. Looking at EUI helps ensure that buildings are "doing their part" independent of the grid, in addition to identifying building-specific risks and benefits.

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## WHAT ARE THE BEST INVESTMENT TACTICS TO REACH DIFFERENT SUSTAINABILITY GOALS?

Achieving each of these objectives entails different investment tactics:

The choice of properties to acquire depends on the specific goals and approach of the investor. For those prioritizing strong GHG performance, the focus may be on ENERGY STAR®–certified, all-electric buildings in cleaner grid areas like California—supplemented by green power purchases to achieve zero emissions. Investors aiming for relative GHG improvement could target median-performing buildings in dirtier grid markets like Colorado, then implement electrification measures, install on-site solar where feasible, and potentially purchase green power. In this scenario, improving property efficiency might be optional if green power proves more cost-effective than capital investments in efficiency upgrades.

For those focused on high EUI performance, ENERGY STAR® certified buildings in any market would be the primary targets. A strategy centered on relative EUI improvement would involve acquiring median-performing buildings across various markets and enhancing their energy efficiency and ENERGY STAR score, without necessarily pursuing full electrification.

### EXHIBIT 4: TACTICAL CONSIDERATIONS FOR EMISSIONS VS. USAGE

| PRIORITY | HIGH PERFORMANCE | RELATIVE CHANGE |
|---|---|---|
| GHG EMISSIONS | • Strict focus on Market selection – dirty vs clean grids (location-based GHG)<br>• Purchase all-electric buildings<br>• Pay premium for green power (market-based GHG) | • Invest in dirty grids and create demand for green power; invest in grids with plans for decarbonization (and look at future energy sources as well)<br>• Implement capital plans to electrify buildings (and select property types that are easier to electrify)<br>• Pursue on-site solar where technically feasible and state policies are in place for power to be sold to tenants or grid |
| ENERGY USE | • Buy, hold, and maintain efficient buildings | • Buy lower performing buildings and integrate efficiency into capital plans<br>• Consider property type dynamics related to data and landlord control |

## WHAT ARE THE BEST METRICS TO MEASURE PROGRESS TOWARDS GOALS?

There are several options to measure progress towards each type of goal:

*GHG Emission Metrics*

For GHG emissions, totals and reduction over time are the most straightforward metrics. Reductions over time can be evaluated annually, over a hold period, since vehicle inception, and/or a since base year.

Investors can also track on-site solar installations in addition to, or instead of, an overall GHG metric. On-site solar is one of the main ways that owners can directly impact GHG in a financially accretive manner.

Some investors are also using the CRREM Pathways, which provide descending annual targets for GHG intensity, broken out by property type, climate zone and grid. The targets are based on the remaining carbon budget allocated to that market segment under a 1.5-degree scenario.[2] These investors are often evaluating "stranding year" or the year when the property's GHG exceeds the remaining carbon budget. While this can be a useful high-level metric, it is important to note that most properties exceed the CRREM carbon budget by the early 2030s. Market-based green power procurement is therefore essential to meeting the CRREM GHG pathways.

### EXHIBIT 5: METRICS FOR DIFFERENT STRATEGIES

| PRIORITY | HIGH PERFORMANCE | RELATIVE CHANGE |
|---|---|---|
| GHG EMISSIONS | • Total GHG<br>• Total on-site solar generation (kW)<br>• CRREM GHG Pathway – average "stranding year" (year above curve) | • Change in GHG intensity over time<br>• On-site solar installations (kWh)<br>• Change in CRREM average "stranding year" |
| ENERGY USE | • EUI by property type<br>• Average ENERGY STAR score<br>• % of SF or AUM with ENERGY STAR certification | • Change in energy use intensity by property type, over time<br>• Change in average ENERGY STAR score<br>• Change in % of properties with ENERGY STAR Certification |

Energy Use Intensity (EUI) is a widely accepted metric globally.

### EXHIBIT 6: CRREM GHG "STRANDING YEAR" BY PROPERTY TYPE ON A CLEAN GRID

| ENERGY STAR SCORE | WAREHOUSE - CALIFORNIA | HIGH RISE MF - CALIFORNIA |
|---|---|---|
| 95 | 2039 | 2031 |
| 75 | 2034 | 2023 |
| 50 | 2024 | 2020 |

*Energy Use Metrics*

For evaluating energy use, Energy Use Intensity (EUI) is a widely accepted metric globally, and should be examined on a property type basis to control for the variations discussed previously.

Moreover, ENERGY STAR® Portfolio Manager is an exceptional resource for sustainable investing in the US, because it is the industry standard tool for tracking, evaluating, and reporting energy performance. The tool tracks utility usage, normalizes for weather and occupancy, and generates key metrics as well as a 1-100 score representing the property's performance relative to the building stock. Investors can examine the ENERGY STAR score of individual buildings, the average score for the portfolio and/or the portion of properties achieving ENERGY STAR certification for performance above the seventy-fifth percentile.

As a public tool that provides benchmarks based on measured performance, ENERGY STAR is perhaps only comparable to NABERS in Australia, since European EPCs are based on physical conditions and modeled data.[3] In general, actual energy performance is usually worse than modeled energy performance, meaning ENERGY STAR is more accurate and stringent than modeled approaches.

## WHAT TYPE OF SUSTAINABILITY TARGET IS BEST?

Investors in real estate must carefully consider their goals when developing sustainability targets, as different objectives can lead to varying approaches.

While some may focus strictly on GHG emissions, this approach often requires investors to allocate capital based on power grids or invest in items that may not have a strong financial business case, such as electrification and green power. For those pursuing carbon budget-based GHG targets in the US, it's crucial to be transparent about their willingness to pay for these items and to consider handling them separately from typical investment return calculations. Alternatively, many investors may find it more appropriate to view NZC as a long-term goal and emphasize GHG emissions reduction progress.

Energy efficiency measures often rival or surpass grid location choices and green energy initiatives in their impact on reducing greenhouse gas emissions. Site energy use is a robust metric for performance evaluation. Real estate owners have greater influence over a property's energy use than its energy sources, and energy use aligns more closely with value generation. Prioritizing energy-efficient buildings can lead to lower operational expenses, enhanced market appeal, and reduced vulnerability to energy price volatility and emerging regulations such as building performance standards.

Investors have options when it comes to building a sustainable portfolio using either metric. They can either acquire properties that are already low-carbon or energy efficient or improve properties through a "brown to green" strategy. The former approach can benefit from tenant and investor premiums associated with best-in-class properties, and the latter approach can drive returns by decreasing OPEX and increasing marketability to tenants and buyers. Either strategy can potentially achieve sustainability goals while also addressing risks and opportunities that can impact financial performance.

Investors can either acquire properties that are already low-carbon or energy efficient or improve properties through a "brown to green" strategy.

## ABOUT THE AUTHORS

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## NOTES

[1] eGRID source "Emissions & Generation Resource Integrated Database (eGRID) | US EPA," US EPA, March 20, 2025, https://www.epa.gov/egrid.

[2] CRREM. "Objectives & Benefits." Last modified 2025. https://www.crrem.eu/objectives-and-benefits/.

[3] Yefei Bai, Cong Yu, and Wei Pan, "Systematic Examination of Energy Performance Gap in Low-energy Buildings," Renewable and Sustainable Energy Reviews 202 (July 5, 2024): 114701, https://doi.org/10.1016/j.rser.2024.114701.