

Real Estate Finance

08

CORE DIFFERENTIATOR

INVESTORS WARM UP TO ESG STRATEGIES

Commercial real estate investors are increasingly eyeing funds that offer ESG lending strategies, with this focus emerging as a differentiator in a crowded market. "It's almost like everyone and their brother is a CRE lender. Therefore, there's been a pushback from pension funds and institutional investors who are asking, 'Why should I invest with you when there are 40 other funds out there doing the same thing,'" said Stuart Boesky, CEO at Pembrook Capital Management. "Now, everyone is looking for something that's different."

Pembrook focuses on affordable housing financing a product type that continues to grow in importance for socially conscious institutions and investors. "I think real estate investors are getting nervous about high-end housing product," Boesky added. "They also seem to understand on a national basis that there's a tremendous housing crisis and that there's a tremendous demand for that product."

An ESG focus, however, isn't the only draw for investors seeking exposure to the sector. "It's been our experience that the people who are really going to allocate and write a check are not solely focused on ESG," Boesky said. "I think they view it as a nice additional feature of what we do, but they wouldn't be investing unless they thought it was the best risk-adjusted return for their money."

Socially conscious real estate is also finding more acceptance in the lending markets, with agency lenders Fannie Mae and Freddie Mac leading the charge. In addition to its affordable housing mandate, the two groups have been pushing hard into the green financing market since 2014, offering incentives for property owners to make green improvements to multifamily buildings.

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Green lending programs at both agencies require owners to achieve at least a 25% cost savings in either water or energy usage. In return, owners receive better pricing and more proceeds on their loans.

"Often, especially on acquisition, the borrower is already planning to execute rehab, so they're likely going to add upgrades [to make a property more efficient] anyway," said Andy Shires, director at Greystone & Co. "So we do the better pricing for what you're doing regardless."

Freddie and Fannie also offer borrowers an Energy and Water Audit Report. Borrowers must have in order to obtain a green loan. Fannie currently reimburses the entire cost of obtaining the report, while Freddie reimburses up to \$3,500.

Investors who work in international markets are also finding that other governments are promoting similar types of lending programs to encourage property owners to make green improvements. Fannie recently launched a C\$182m program that provides grants to Canadian organizations that are increasing energy efficiency in built and existing properties.

London has also spent the past several years promoting RE-FIT, a program that hopes to improve energy efficiency and reduce carbon in non-residential buildings. The program allows borrowers to keep 100% of their energy savings, which are typically between 15% and 20% (see page 9 for a full breakdown of the lending programs).