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CASE STUDY:

Colony NorthStar's Plan to Win With Sustainable Real Estate

A conversation with Ryan McManus of Colony NorthStar

With commentary by Dan Mistler of EY

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Ryan McManus
Senior Vice President,
Colony NorthStar

Few industries on earth have more of an impact on the environment than real estate. One of the biggest real estate investors in the world, Colony NorthStar, has a plan to decrease its own carbon footprint while driving real investment returns. At Privcap's Private Equity ESG Summit, the firm's head of sustainability, Ryan McManus, shared details of that plan.

With $58B in assets under management and 500 employees, Colony NorthStar utilizes the EPA's Energy Star tool to track a series of performance indicators across its vast portfolio. The firm also uses the U.S. Green Building Council's LEED certification as an important marker of sustainable real estate.

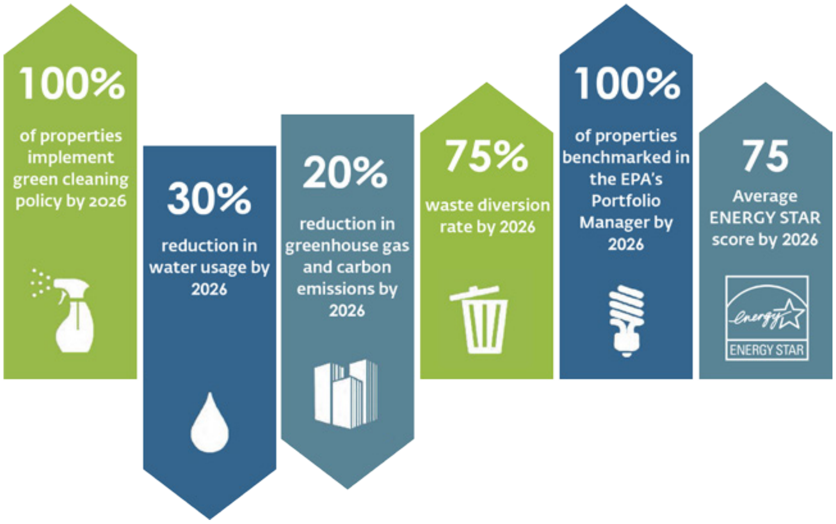
And the firm is seeing results. In 2016, its first year of reporting, Colony was ranked second globally among real estate debt investors by GRESB (Global Real Estate Sustainability Benchmark), the industry standard for assessing sustainability in real estate.

Privcap: How new is the idea of sustainability within the real estate investment industry?

Ryan McManus, Colony NorthStar: Sustainability in real estate is not exactly new, but the formalization of the process and the emergence of building certifications have accelerated in the last 10 to 15 years. Fast-forward to today and there are over 15 billion square feet of LEED-certified buildings across the world, in every major marketplace. Reporting is becoming more standardized making it easier to measure sustainability performance of both properties and their parent companies alike.

What is your role at Colony NorthStar?

McManus: I oversee fund operations and investor reporting for the firm's private equity real estate funds, as well as the implementation of ESG initiatives throughout our portfolio. The two areas are complimentary. Knowing what is important to our investors has helped us shape a successful ESG program.



Colony NorthStar's ESG Goals

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What was behind Colony NorthStar's desire to formalize an ESG program?

McManus: First, sustainability is good business, and that's as clear for real estate as any other asset class. Reducing your energy and water consumption helps lower operating costs. It's also positive on the revenue side in terms of facilitating higher rental premiums for tenants who want to occupy green buildings. Additionally, energy efficient buildings have been proven to also have better terminal values and superior cap rates. These are among the many financial benefits we've experienced in our own portfolio.

Secondly, ESG is a critical component to any risk management program. We need to understand and monitor our environmental and regulatory risk.

And lastly, it's a matter of stewardship. Real estate accounts for an enormous amount of our global energy consumption and water consumption and waste output. In the U.S. alone, real estate accounts for around 40 percent of carbon emissions. That's more than the industrial sector, more than transportation, more than agriculture. So we've looked at that opportunity. If we can move the needle just a little bit, then we can have a great impact.

What is an example of a strategy that has cut costs and also had an ESG impact?

McManus: On the water side, last year we converted one of our very water-thirsty properties that had 64,000 square feet of lawn landscaping into mulch and drought-resistant vegetation. In California, this matters a great deal. That initiative is saving 1.6 million gallons of water a year, which is very important to our resources and to our bottom line.

Would you consider buying an energy-inefficient property and converting it into a more sustainable asset?

McManus: That's very much in play. Our ESG principles are not meant to be a barrier to investment; rather, we intend to identify risks and opportunities down the road. Through our active asset management plan and refurbishment and upgrading of the building facilities, we are making our properties more efficient. It takes a lot of human capital. It takes investment capital. But there is a positive return on that. ■

The Power of Standards

Dan Mistler
Senior Manager, Climate Change and Sustainability Services, EY

Mistler explains why ESG benchmarking tools are becoming more widely used

"The identity of ESG is changing from something that felt fluffy to something that funds can really make money with. That progress has been about the ability to draw a business case between ESG interventions and business outcomes.

"One of the things that is needed is a bit more standardization, particularly with KPIs. There are some external frameworks being developed that a firm can take and build off of. For example, the Sustainability Accounting Standards Board, or SASB, is developing a great framework that is sector-specific. SASB guidance is really about understanding the materiality of the risks that the business may be facing, given the geography and the business sector it is in.

"In real estate, energy usage has been a recognized issue for much longer than in some of these other industries. The Energy Star program is a perfect example of that. Energy management is a great example of the easiest ESG initiative that you can have in a portfolio."