

Preserving & Improving Assets

Navigating the sustainability maze

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 **JLL** SEE A BRIGHTER WAY

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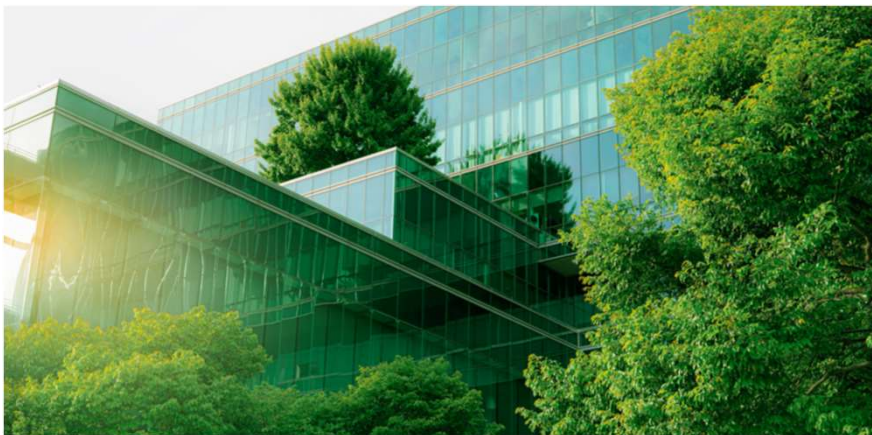
Noah Lee
Senior Associate
The Americas

JLL

Sustainability at the forefront of our thinking

Our global sustainability program

JLL's sustainability program is focused on delivering impact on three key areas: Climate action, Healthy spaces and Inclusive places. We call this our Sustainability Framework, with each area supported by specific targets. The implementation of the program is supported by a global governance structure for sustainability.



JLL partners with Energy & Environment Alliance

JLL is building a future-oriented advisory with coalition partners Energy & Environment Alliance



The Energy & Environment Alliance (EEA) is a not-for-profit coalition of hospitality sector leaders to achieve new vision of the world – one which is green, sustainable, and where everybody can prosper. The EEA is developing the first universal sustainability standard for hospitality buildings and operations, in collaboration with investors, asset owners/managers, experts and its strategic partner BREEAM, the world's most reputable sustainability assessment method for master-planning projects, infrastructure and buildings.

Navigating the sustainability maze

Introduction to JLL's latest research paper*

“ESG is a huge value preservation opportunity. It focuses the attention of the investor on ensuring value retention and value creation. The valuation of the asset is absolutely critical in that mix.”

Ufi Ibrahim
Chief Executive Officer
Energy & Environment Alliance

- The world continues to prioritise sustainability and combat climate change
- Tourism accounts for c. 8% of global carbon emissions, with the hospitality industry constituting a significant part of this
- Hospitality sector has a crucial role to play in achieving a net zero carbon (NZC) future

*<https://www.jll.co.uk/en/trends-and-insights/research/navigating-the-sustainability-maze>

It's all about data

Alignment across the industry

- Growing momentum around regulatory frameworks for ESG reporting
- The CSRD¹ and ISSB² standards aim to align reporting standards for ESG matters
- IVSC³ and RICS⁴ provide guidance on incorporating ESG into valuations
- Challenges in accessing quality data in the hotel sector
- Difficulty reflecting the risk of stranded assets without reliable ESG data
- Larger companies are leading ESG initiatives, while smaller businesses need support
- SMEs require education and support to meet ESG regulation and stakeholder demands

1: CSRD = Corporate Sustainability Reporting Directive
3: IVSC = International Valuation Standards Council

2: ISSB = International Sustainability Standards Board
4: RICS = Royal Institution of Chartered Surveyors

"... it's about transparency and having a road map aligned with the Paris agreement including KPIs."

Caroline Tivéus
Director of Sustainable Business
Pandox

	 Carbon emissions	 Physical risk	 Health and wellbeing	 Biodiversity	 Waste management	 Community impact/relations	 Voluntary certifications
Data	✓	✓	✓	✓	✓	✓	✓
IVSC	✓	✓	✓	✓	✓	✓	✓
RICS	✓	✓	✓	✓	✓	✓	✓
BBP	✓	✓	✓	✓	✓	✓	✓

The list is not exhaustive.
Source: JLL Research

Guest behaviour

Pushing performance and values through implementation of measures

Opportunities

- Gen Z prefers sustainable brands and is willing to pay more: Booking.com reports 75% of travelers want to travel sustainably
- Investment in NZC can boost rates/occupancy
- Corporate travel policies improve visibility of green certifications and push hotels to implement and demonstrate ESG measures
- Transparency is important for driving consumer behaviour change: Booking.com removes self-certified labels for transparency
- Actual booking data can support trading: positive impact on values through enhanced cashflows

Challenges



Intention-Behaviour Gap

- Gap between consumer intentions and spending behaviour: prioritisation of travel experience over sustainability
- Sunken cost fallacy affects willingness to overlook emissions
- 28% prioritise time over sustainability in decision-making



Transparency/Greenwashing

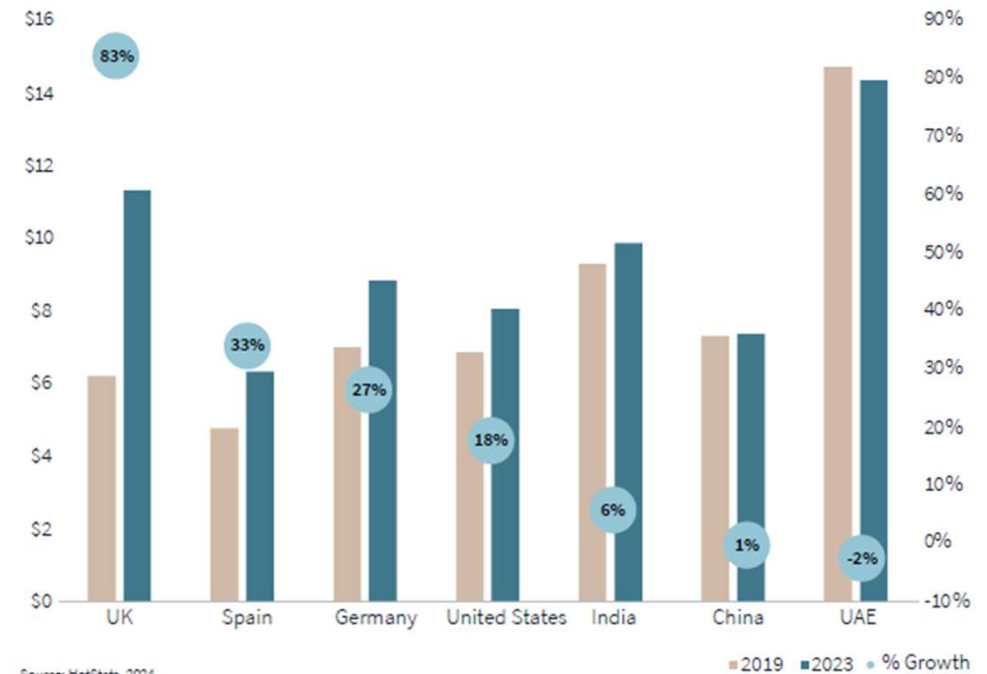
- ESG investment's impact on performance requires guest visibility and trust
- Many 3rd certifications have little meaning to guests on booking platforms
- Some certifications neglect real estate aspects and lack correlation with CO₂ emission reduction
- Focusing on impactful initiatives is crucial for emissions reduction
- Lack of transparency and industry-wide certifications can lead to greenwashing and consumer distrust/limited understanding

Energy price increases

Improvement of energy efficiency needs to be in the focus

- Sustainable hotels can increase profit margins through improved energy efficiency
- Energy audits, lighting upgrades, HVAC optimisation, water conservation, renewable energy, and guest engagement are crucial for sustainability
- Rising energy prices globally make energy efficiency even more important
- Increased utility costs impact hotel values
- Efficient investments in plant and machinery can lower utility costs, leading to improved profit margins
- "Green premium" refers to the value preservation and potential increased value of a sustainable hotel asset

Total utility costs per available room



Design & building improvements

Contribution to ESG targets and potential reduction of operational costs

- Improvements in building design make hotel buildings more economically and environmentally viable
- Existing hotel buildings incorporate improvements during planned maintenance and refurbishment works
- Each solution is assessed for CAPEX, contribution to ESG targets, and potential operational cost reduction
- Replacement of plant and equipment depends on condition, remaining service life, and sustainability objectives
- New developments incorporate sustainability measures from the start, such as achieving BREEAM¹ Excellent or Outstanding ratings
- Design solutions include onsite energy generation, water capture, maximising natural light, and using higher thermal performance materials and energy-efficient equipment

Focus of measurements



Thermal insulation upgrades

Replacing existing windows, upgrading insulation on existing external walls, and adding new or replacing existing roof insulation



Fully integrated building management system (BMS)

to improve energy efficiency of the whole building



Solutions that limit disruption

to occupied properties whilst providing improved performance to include lighting replacement to LED with sensors and dimming capability

1: BREEAM = Building Research Establishment Environmental Assessment Methodology

Green financing

Appetite is strengthening

- Debt market's focus on ESG is important for integrating sustainability into investment decisions
- Green financing and green loans are becoming more prevalent, providing funding for projects with positive environmental benefits
- US\$4.4 billion of global impact bonds have been issued, with a majority in the past three years
- Institute of International Finance expects global ESG-related debt to reach US\$7 trillion by 2025
- The hotel industry has seen increased adoption of green financing in recent years
- Europe is expected to lead in sustainability initiatives due to stringent regulations
- Sustainability-linked loans require performance improvements for more favourable debt terms

“Today we have approximately €200 million in sustainability-linked loans which will double within a couple of months. Banks in the Nordics are pushing to convert existing facilities into green loans – in a couple of years this will be a hygiene factor to get refinancing.”

Caroline Tivéus
Director of Sustainable Business
Pandox

Reflection in hotel transactions

ESG has gained prominence in underwriting of deals

- Limited recent transactions and inconsistencies in evaluating ESG risk hamper the evidence of ESG considerations impacting hotel transaction prices
- ESG-related due diligence, especially regarding climate risk and energy performance, is gaining prominence in hotel transactions
- Some market participants are testing whether ESG investments yield premium prices on exit
- Increased communication, data collection, and standardisation are crucial to avoid mispricing of assets in the long term
- Mispricing of assets due to neglecting ESG risks could lead to a larger impact in global financial markets
- Failing to meet sustainability standards can result in price chips in hotel transactions



“We have seen few examples of green premiums for hotel transactions because it is difficult to isolate these factors. However, price chips as a result of failing to meet sustainability standards are becoming more common.”

Rekha Toora
Senior Vice President
EMEA Hotels & Hospitality
Capital Markets JLL

Impact on cashflows & values

A question of when, not if to be seen – a case study

- DCF¹ methodology helps valuers analyse the impact of NZC investments on cash flow and hotel value
- Regulated valuations reflect existing evidence of NZC investments, focusing on energy cost savings
- Risk analysis considers forward-looking factors like consumer behaviour and discount rates but may not influence regulated valuations without transactional evidence
- Sustainability-focused CAPEX schemes can increase values in regulated valuations
- Business cases and expert advice are key for reflecting value uplifts in regulated valuations

1: DCF = Discounted Cash Flow

Category	Regulated valuation		Risk analysis*	Explanation
	Base case	Green case	Green case	
CAPEX	€0m	€2m	€2m	
Occupancy	85%	85%	86% ↑	Changes in guest behaviour may be reflected in risk analysis scenarios, but are unlikely to be reflected in regulated valuations at the moment.
Total revenue	€13.3m	€13.3m	€13.5m ↑	
Utility costs %	4%	2.5% ↓	2.5%	Valuer likely able to reflect impact of NZC CAPEX investment on Utility costs within DCF.
EBITDA (%)	5.15m (39%)	€5.30m ↑ (40.5%)	€5.37m ↑ (40.5%)	
Exit yield	6.00%	6.00%	5.85% ↓	Change in exit yields and discount rates may be reflected in risk analysis scenarios. For regulated valuations, they are currently unlikely to be reflected given lack of evidence.
Discount rate	8.00%	8.00%	7.85% ↓	Depending on payback period of investment, a positive impact of NZC CAPEX may be reflected in both risk analysis and regulated valuations.
Gross value	€82m	€85m ↑	€88m ↑	
Capital value	€82m	€83m ↑	€87m ↑	

*Exemplary calculation only. Regulated valuations are based on current market evidence, while risk analysis may base its metrics on future sentiment and anticipated future market conditions.
Source: JLL Hotels & Hospitality Group

In summary...

Collaboration remains key in accelerating towards a NZC future

- Data alignment is on the way
- Transparency and trust in sustainability certifications need improvement
- Consumer behaviour changes and the intention-behaviour gap difficult to reflect in performance forecasts
- Energy efficiency is crucial, with investments leading to cost reductions and, hence, performance and value improvements
- Green financing options are gaining traction, particularly in Europe
- Transactional evidence still somewhat limited, hence, there is a lack of sufficient evidence of the impact of ESG credentials in trades
- Education, data transparency, standardisation, and collaboration are key to effectively reflect the risks and opportunities of NZC for the hotel sector

“It’s important to choose the right tenants and the right brands which have a strategy that is aligned with yours, that transparently share data and are willing to align targets and work towards common goals.”

Adrian Flueck

*Director of Hotel Investment Management
Invesco Real Estate*

Thank you very much!

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Head of DACH

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