ESG AND THE FUTURE OF HOSPITALITY

PART 2: Creating Value
Part One of this series looked at how Environmental, Social, and Governance (ESG) is influencing the hospitality industry, and how sustainable design solutions can lead to reduced costs, increased revenue, and satisfied stakeholders. Part Two will take a deeper dive into the investment landscape, and how ESG can build value for hotel assets.

The post-pandemic travel boom shows little sign of slowing. Following a survey, Expedia considered 2022 the year of the GOAT, or “the greatest of all trips”, with 65% of respondents planning to “go big” the next time they travel. Asset sales are also expected to increase in the industry. Over the next three years, $31 billion of hotel debt will mature in the U.S. Although lenders have been lenient throughout the pandemic, the extensions are not expected to continue, and property owners are more likely to sell.

Environmental, Social, and Governance will play a significant role in the value of hotel assets as private equity (PE) firms return as the dominant hotel buyers. In 2021, PE firms were responsible for 48% of global hotel transaction volume, totaling USD $31.7 billion. Their increasing focus on ESG has the potential to change how hotel assets are valued.
As touched on in Part One of this series, investors have stricter expectations of assets as it relates to ESG. In PwC’s recent Global PE Responsible Investment Survey, 37% of respondents said they have refused an investment opportunity because of ESG concerns. Governance has been a priority factor for PE firms since their beginning. Environmental, now, is also a focus for PE firms as it has become easier to quantify as well as communicate with certifications, metrics, and standards. The social aspect, due to its difficulty to quantify, is still lagging.

That’s not to say that a holistic ESG approach is unexpected. Across industries, people are considering how we can use private capital for the public good. INSEAD’s Global Private Equity Initiative surveyed the largest asset owners, and found that 90% of them factor ESG into their investment decisions. 48% of PE firms report taking action on the carbon footprint of their portfolio companies. As more investors are adopting the United Nations Principles for Responsible Investing, social impact returns are increasingly intriguing to them, and social investments are becoming their own asset class. All of this is to say that the value of every portfolio is now—most likely—being assessed by ESG issues. This approach is on its way to becoming an industry standard.

Research investment firms provide the tools needed to assess portfolios based on ESG. Their evaluation of the characteristics of properties in turn offers insight into how an investor might consider their portfolio. In some cases, an investor might approach a research investment firm with certain expectations of ESG in mind, whether that’s LEED certification, net zero carbon, or operational requirements.

In order to increase the value of an asset, there must be an ESG report attached that speaks to how the building is futureproofed for climate change, as well as energy efficient. However, ESG is a recent standard, and there isn’t quantitative historical data that typically informs a property, like how flood scores will determine projections. We’re only at the tip of the iceberg, and with this, there’s opportunity for firms to become thought leaders in the industry and shape how we approach, model, and measure ESG.

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Sustainability is in many ways the most straightforward part of ESG to quantify. With this, sustainability is no longer a symbol of corporate ethics on display, but a key part of a financing plan. Investor partners are keeping close tabs on the metrics of the environmental performance of new properties. Existing non-sustainable properties will become increasingly difficult to sell as part of a larger portfolio, and are at risk of becoming stranded assets. It’s projected that trillions in assets will become stranded in response to the anticipated impacts of the climate emergency. A large portfolio of stranded assets not only will become unsellable, but will also limit the ability to raise funds, as well as affect credit ratings, and insurance premiums. On the other hand, if you’re looking to exit a property, an ESG approach will attract a wider range and quality of investors, clients, and transactional partners.
For properties at risk of becoming a stranded asset, there are ways in which to create a more sustainable building, track its metrics, and increase its value, ultimately making it easier to sell. In Madrid, we improved the envelope of an existing project so that it better regulates indoor conditions and provides better daylight, emits less carbon, and even generates its own energy. The project, originally built in 1990, needed upgrading. Rather than demolish the building, a careful design upgrade for the façade created a high-performance envelope, with photovoltaics generating its own energy and a bioclimate system exposed to the sun that included glass slats for solar protection.

By using the same structure instead of demolishing it, 8,937 metric tons of carbon embodied in the concrete structure stay in the building and out of the atmosphere. If this is annualized for a 60-year lifetime of the building, this represents a reduction in emissions of 148,953 kg CO2e. By improving the envelope and the mechanical systems and adding generation of renewable energy by integrating photovoltaics in the facade and roof top, a reduction of 49% in the annual energy use compared to the 2003 baseline is achieved. This is reflected in the operational carbon as a savings of 101,151 kg CO2e per year. Assuming an additional building life of 60 years and no further improvements in the envelope or decarbonization of the grid, the annualized savings in carbon are 250,104 kgCO2e in operational carbon per year. This is equivalent to adding 4,134 tree seedlings every year, grown over 10 years.
In Part Three of this series, we will discuss the strategies and solutions that will allow hotels—both new developments and existing buildings—to attract the new generation of guests, talented staff, and investors, while preparing for the uncertainties of the future.

It’s now an expectation that new development will be sustainable, while taking into account visitor experience, and the impacts of the development on the local community. For the Grand Hyatt Kuwait, CRTKL took advantage of advanced sustainable design and construction to develop a high-performing property. The hotel is positioned on the southwest corner of the 360 Mall expansion, exposing it to the intense afternoon sunlight, with summer temperatures reaching 46°C (116°F). The design of the hotel’s facades passively combats solar heat gain and addresses the poor solar orientation of the site and the effects of the region’s harsh climate. Initially incorporated as an external shading device, the screens’ design evolved to be much more than a simple reducer of the solar heat gain from large swaths of glazing. The team studied the percentage of openings and module scales and developed a gradient pattern that transitions from entirely opaque at the screen’s top to 75% open at eye level. This design provides adequate shade on the glass while maintaining guest views from the interior and light filtration throughout all of the hotel’s public spaces. The parametric pattern was utilized in various ways across the exterior, maintaining a consistent design aesthetic while providing a necessary purpose, combating the intense summer heat in the region.

An approach to ESG not only reduces long-term risk of investments, but also allows hotels to diversify their investor base and add value to properties. In short, ESG is not only good for portfolios, but also for the environment, and it’s improving our lives.

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Clay Markham  
**Principal | AIA, LEED AP BD+C**

Clay leads the hospitality sector with a dynamic design and management approach to architecture, interior design and construction management. With over 40 years in the industry, Clay has worked extensively on international and domestic projects, allowing him to apply diverse market experiences to a variety of project types from single-use environments to large-scale master plans to mixed-use projects. His compelling designs and successful project delivery skills have resulted in award-winning projects for individual developers and owners as well as top-tier brands including Marriott International, Hyatt Hotels and Resorts, and InterContinental Hotel Group.

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Todd is an Director with CRTKL, leader of the firm's regional Commercial Practice Group for Europe and the UK. Having relocated to the London office in August 2011, Todd will build on over three decades of experience as a recognized expert in the planning and design of mixed-use and hospitality driven environments and developments. His extensive worldwide experience from Asia, to Europe and the Middle East, Latin America and North America, covers the full spectrum of hotel brands and includes convention hotels, boutique resorts, extensive property repositioning, renovations and master planning as well as multiple significant mixed-use projects.

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Leading CRTKL's Performance-Driven Design℠ initiatives, Pablo is a recognized leader in green design. His expansive portfolio includes sustainable buildings all over the world designed with state-of-the-art tools and green strategies. Pablo is a tenured professor of Architecture at Cal Poly Pomona University. He has been published more than 130 times, including notably Carbon Neutral Architectural Design by CRC Press currently with a second edition published in July of 2017.

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