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Task Force on Climate Change financial disclosures (TCFD) in the real estate industry

Deloitte Advisory (Hong Kong)

MAKING AN IMPACT THAT MATTERS since 1845

Task Force for Climate-related Financial Disclosure (TCFD)

“As a priority, to enhance listed companies' reporting of environmental information emphasizing climate-related disclosure, taking into account the Mainland's policy direction to target mandatory environmental disclosure by 2020, and aiming to align with the TCFD recommendations.”

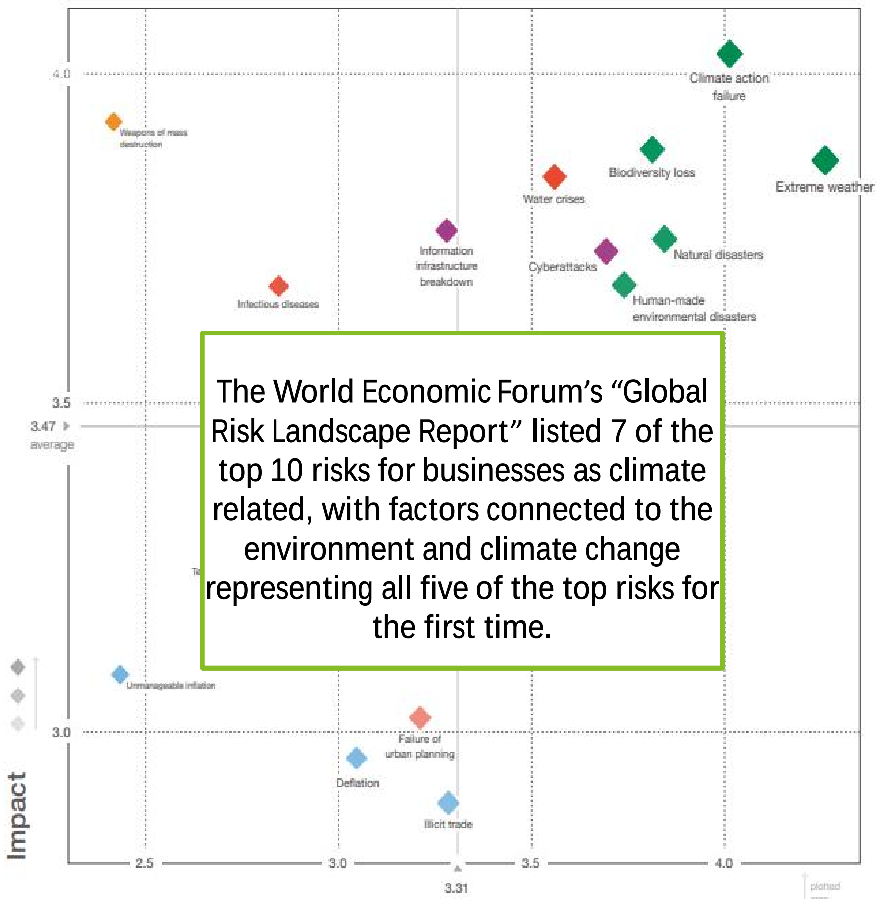
SFC, *Strategic Framework for Green and Sustainable Finance (Published on 21 September 2018)*

Climate change is the leading risk of the global economy

One illustration: the World Economic Forum 2020 Global Risks Report

The Global Risks Landscape 2020

What is the impact and likelihood of global risks?



The World Economic Forum's "Global Risk Landscape Report" listed 7 of the top 10 risks for businesses as climate related, with factors connected to the environment and climate change representing all five of the top risks for the first time.

Top 10 risks in terms of Likelihood	Top 10 risks in terms of Impact
1 Extreme weather	1 Climate action failure
2 Climate action failure	2 Weapons of mass destruction
3 Natural disasters	3 Biodiversity loss
4 Biodiversity loss	4 Extreme weather
5 Human-made environmental disasters	5 Water crises
6 Data fraud or theft	6 Information infrastructure breakdown
7 Cyberattacks	7 Natural disasters
8 Water crises	8 Cyberattacks
9 Global governance failure	9 Human-made environmental disasters
10 Asset bubbles	10 Infectious diseases

Environmental · Geopolitical · Societal · Technological · Economic

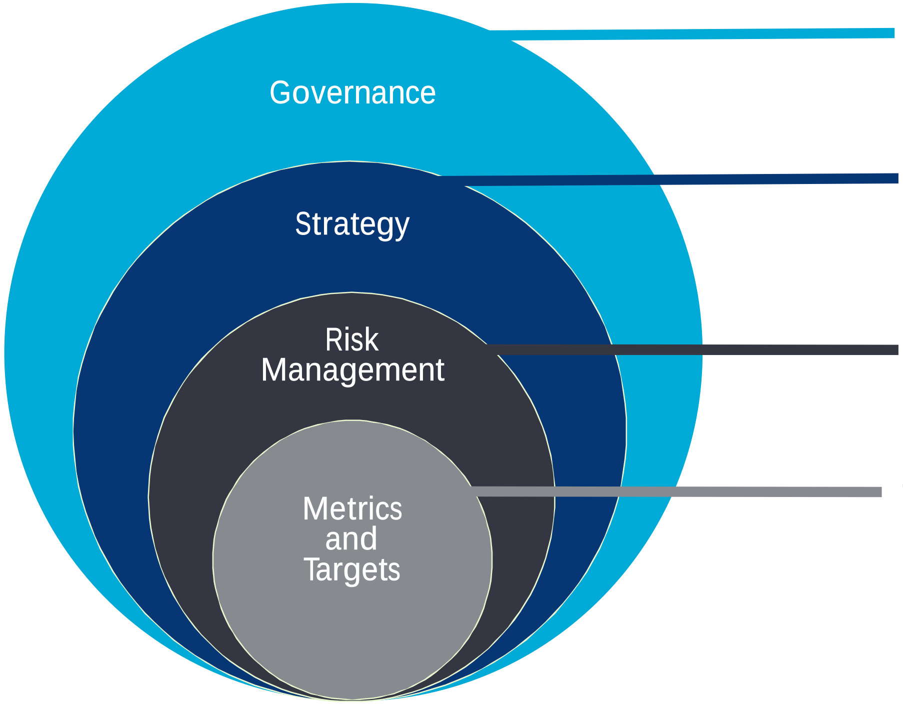
Source: World Economic Forum Global Risk Report 2020

International ESG Reporting Standards

Task Force for Climate-related Financial Disclosure (“TCFD”)

TCFD aims to promote more informed investment, credit, and insurance underwriting decisions and to enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system’s exposures to climate-related risks.

The recommendations are structured around four thematic areas that represent core elements of how organisations operate:



The organization’s governance around climate-related risks and opportunities

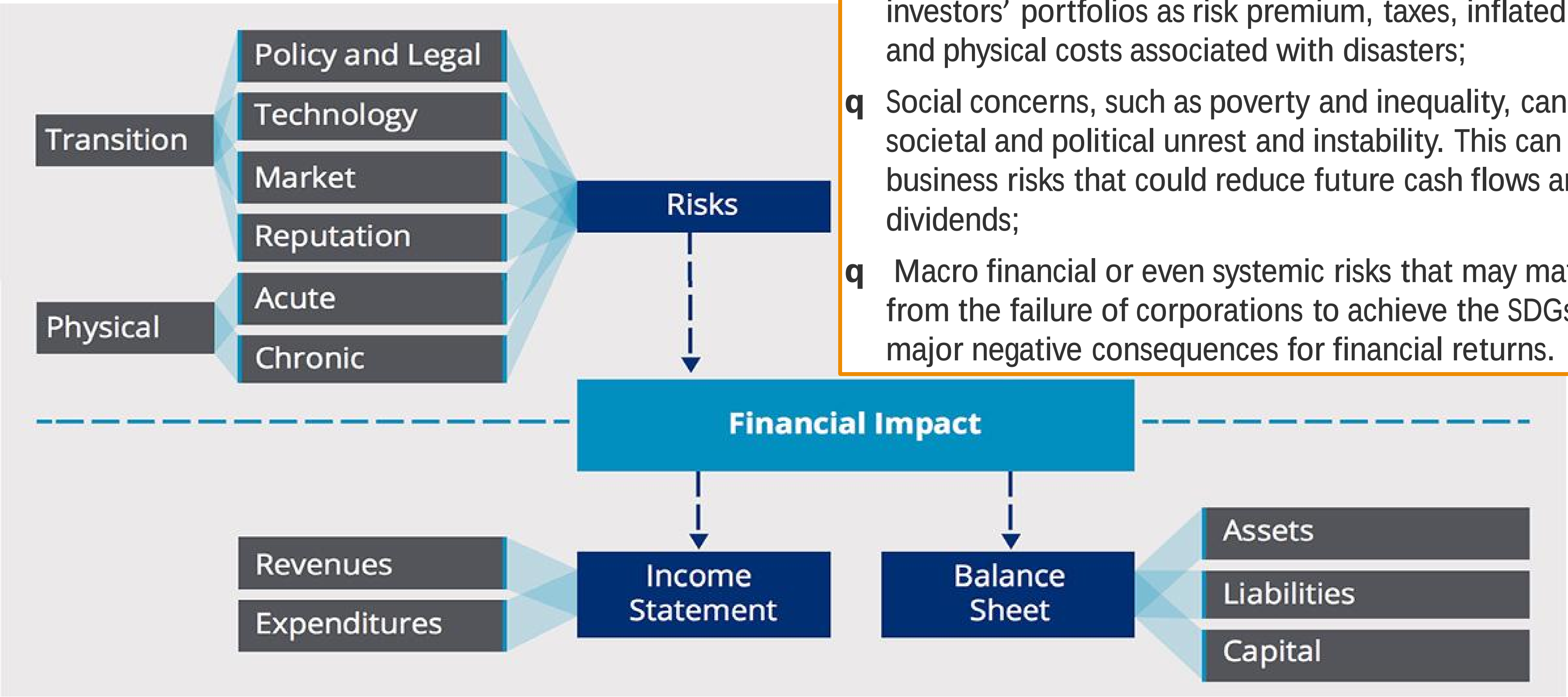
The actual and potential impacts of climate-related risks and opportunities on the organization’s businesses, strategy, and financial planning

The processes used by the organization to identify, assess, and manage climate-related risks

The metrics and targets used to assess and manage relevant climate-related risks and opportunities

TCFD – Focus on Financial Impacts

Taxonomy



- The costs from environmental or climate-related events that have been identified as universal concerns will come back into investors' portfolios as risk premium, taxes, inflated input prices and physical costs associated with disasters;
- Social concerns, such as poverty and inequality, can lead to societal and political unrest and instability. This can also create business risks that could reduce future cash flows and dividends;
- Macro financial or even systemic risks that may materialize from the failure of corporations to achieve the SDGs could have major negative consequences for financial returns.

Financial Impact by Industry

Tail risks

The TCFD has grouped financial impacts from climate-related risks into the following general categories :

- Revenues
- Expenditures
- Assets and Liabilities
- Capital and Financing

For property sector, transition risks may arise from all four major categories – larger shifts in asset values, higher costs of operation, violation of ESG-related laws and regulations and resulting fines, etc., when moving towards a less polluting, greener economy.

It requires property corporates to develop a robust strategy that is integrated into the overall business strategy. While the strategy must retain a level of flexibility, it must also be actionable and measurable.

Evidence of Financial Impact

Groups and Industries		Revenues	Expenditures	Assets and Liabilities	Capital and Financing
Financial	Banks	■		■	
	Insurers	■	■	■	
	Asset Owners	■		■	
	Asset Managers	■		■	
Energy	Oil and Gas	■	■	■	■
	Coal		■	■	■
	Electric Utilities	■	■		■
Transportation	Air Freight		■		■
	Passenger Air Transportation		■		■
	Maritime Transportation		■		■
	Rail Transportation		■		■
	Trucking Services		■		■
	Automobiles and Components	■	■		■
Materials and Buildings	Metals and Mining		■		■
	Chemicals	■	■		■
	Construction Materials	■	■		■
	Capital Goods	■	■		
	Real Estate Management and Development	■	■	■	■
Ag, Food, and Forest	Beverages		■		■
	Agriculture	■	■	■	■
	Packaged Foods and Meats		■	■	■
	Paper and Forest Products	■	■	■	■

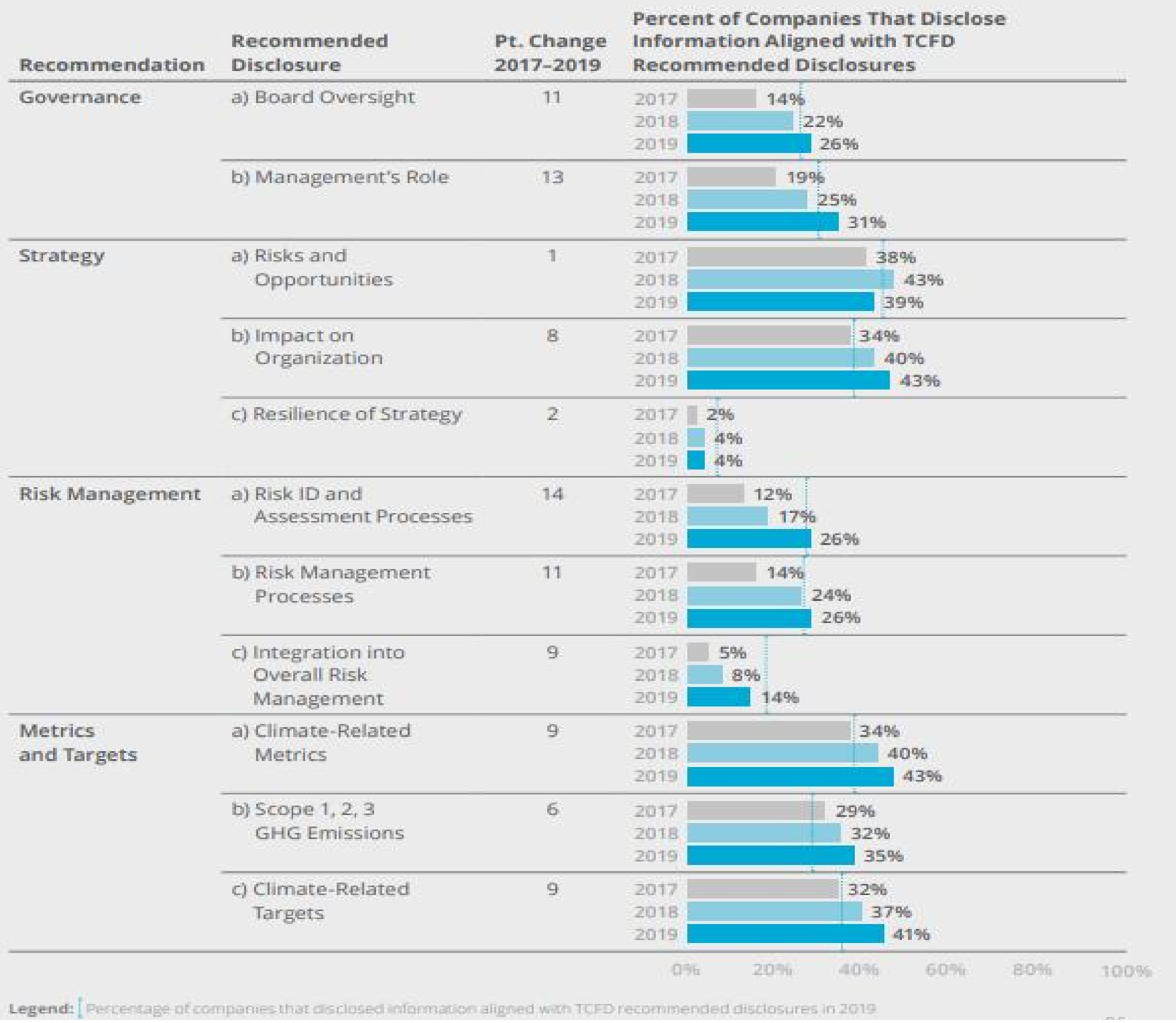
TCFD – 2020 Status Report

PROPERTY SECTOR
BY THE NUMBERS

>1,500 Organisational supporters since TCFD recommendations were published in 2017

Energy companies and materials and buildings companies are leading on disclosure, with an average level of TCFD-aligned disclosures of 40% for energy companies and 30% for materials and buildings companies in fiscal year 2019.

Figure A3-5
Materials and Buildings Review Results



Thinking through investment decisions – Property sector

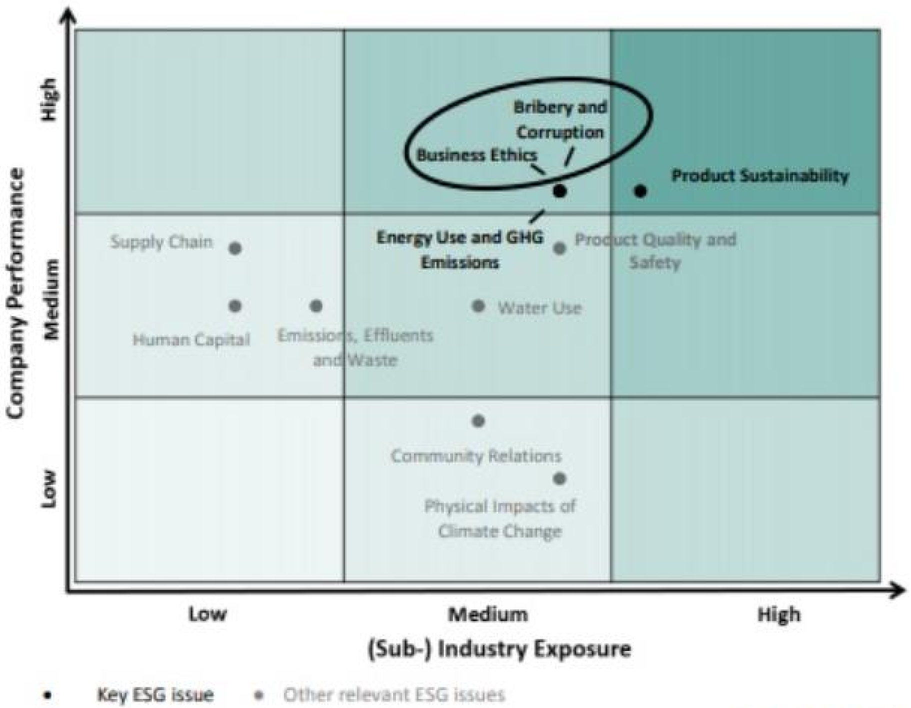
Financial risks of "Brown Assets" (as opposed to "Green Assets", assets without sustainability elements)
The Real Estate industry has made significant strides in recent years to improve its Environmental, Social and Governance (ESG) performance. Notable efforts have been made in Green Building and transparency of operations through broader and more detailed financial and sustainability disclosures.

Despite this momentum, company inertia and systemic governance challenges are preventing the Real Estate industry from meeting its full ESG performance potential. Below captures some most commonly concerned area for the Real Estate industry in investment decision making.

"what will happen to the 30-year mortgage – a key building block of finance – if lenders can't estimate the impact of climate risk over such a long timeline, and if there is no viable market for flood or fire insurance in impacted areas?"

-- 2020 letter to CEOs, Larry Fink, CEO, BlackRock

Materiality Matrix – Real Estate



Source: Sustainalytics, 2015

<u>Three material issues are distinguished by their large impacts:</u>

Energy Use and GHG Emissions

- Ø One of the largest consumers of energy and sources of CO_2
- Ø Rising energy costs, volatile fossil fuel prices and prospect of carbon regulation

Product Sustainability

- Ø Green Building

Business Ethics

- Ø Bribery and corruption during land acquisition and development tender
- Ø significant legal, reputational and financial costs

Common ESG Topics among Property corporates

ESG disclosure frameworks & Most reported topics

TYPE	TOPIC	FREQUENCY OF USE
Environmental management: Average disclosure rate 44.6%	Environment management system certification	49%
	Environmental management objective	81.6%
	Policies on energy conservation and renewable energy application	77.7%
Environmental data: Average disclosure rate 35.2%	Energy consumption and conservation	39.4%
	Tailpipe emission and reduction	38.9%
	Wastewater discharge and reduction	46.4%
	Hazardous waste discharge and reduction	36.3%
	Waste recycling	39.9%
Social: Average disclosure rate 28.9%	Number of employees receiving vocational training each year and duration	66.1%
	Donation	88.7%
	Prohibition of forced labour	32.6%
	Prohibition of child labour	32.3%
	Anti-discrimination	41.7%
	Number of female employees	35.5%
	Occupational health and safety	85.4%
	Fatality rate	54.7%
	Lost time rate in accidents	38%
Governance: Average disclosure rate 66.3%	Compensation of directors	97.4%
	Ratio of average compensation of employees and CEO compensation[36]	97.7%
	Separation of President and CEO	97.6%
	Diversity of board of directors	75.8%
	Independence of board of directors	97.2%
	Independent remuneration panel	82.9%
	Independent audit committee	88.4%
	Independent nominating committee	86.4%
	Thematic committees[37]	80.5%
	Unqualified audit report	95.2%

Source: Syn Tao Green Finance, 2018.

ESG disclosure may be structured both by mandatory disclosure requirements and by voluntary guidance by stock exchanges. The lack of standards and confusion of frameworks may impede the quality of ESG data hence hinder ESG reporting.

To meet the growing demand for ESG KPI reporting, and be more transparent and accountable to its stakeholders, thereby increasing trust, corporates may set goals and strategies using parameters from both HKEX's ESG Reporting Guide and the GRI Standards:

HKEX ESG Reporting Guide Content Index

§ Per the requirements of the Environmental, Social and Governance Reporting Guide set out in Appendix 27 of the Main Board Listing Rules and Appendix 20 of the GEM Listing Rules (ESG Reporting Guide) of Hong Kong Exchanges and Clearing Limited (HKEX)

GRI ("Global Reporting Initiative") Content Index

§ Globally accepted standards, provides a common language and credible set of disclosures for organizations to communicate effectively about their impacts on the economy, the environment, and society

§ Includes additional reporting requirements recommendations, and/or guidance that relate to each disclosure

Common ESG KPIs among Property corporates

Primary "E" and "S" indicators

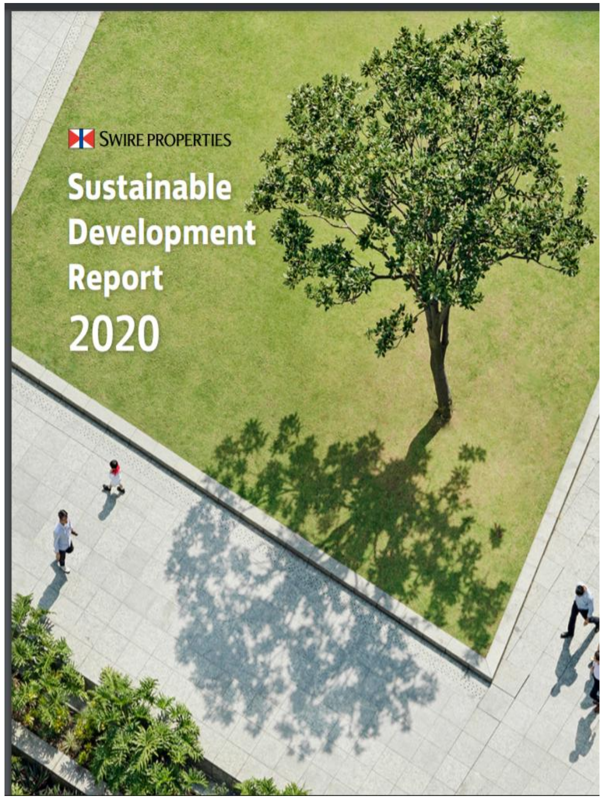
ESG TOPIC	RELATED INDICATORS	FREQUENCY OF USE IN MARKETS	FREQUENCY OF REPORTING REQUIREMENTS
GHG emissions	GHG emissions (scope 1,2) in tonnes GHG intensity (GHG/sales)	92%	68%
Water use	Water used (m^3) % of water recycled % of water used in water stress areas Water intensity (water use/sales)	92%	63%
Energy efficiency and mix	Energy consumed (GW) % of renewables Energy intensity (energy consumed / sales)	85%	64%
Waste (water, solid, hazardous)	Waste from operations (tonnes) % of hazardous waste % of waste recycled Waste intensity (waste / sales)	77%	87%
Workforce composition and diversity	Workforce composition by gender	69%	40%
Employee health and safety	Injury rate (TRIR) and fatality rate for direct and contract employees	100%	84%
Recruitment / Turnover	Voluntary and involuntary employee turnover rate by major employee category	62%	24%
Collective bargaining agreements	% of active workforce covered under collective bargaining agreements	62%	30%

Sustainability indices and benchmarks
- An example of a leading blue chip real estate developer

Sustainability Rating	Year	Rating
Hang Seng ESG 50 Index	2020	–
Hang Seng Corporate Sustainability Index Series (HSSUS)	2020-2021	Hang Seng Corporate Sustainability Index Series Member 2020-2021
Global Real Estate Sustainability Benchmarks (GRESB)	2020	78 / 100 GRESB 2020
MSCI ESG Index – BB Rating	2019	MSCI ESG RATINGS BB (CCC, B, BB, BBB, A, AA, AAA)
Sustainalytics ESG Risk Ratings	2020	17.0 Low Risk (Negl. 0-10, Low 10-20, Med. 20-30, High 30-40, Severe 40+)

Frequency of use represents a selection of E & S metrics with high reporting frequency (IFC, Beyond the Balance Sheet, 2018). The reporting requirements column shows the percentage of countries out of 70 included in the Reporting Exchange database with reporting requirements on the subject matter, including national frameworks (WBCSD, The Reporting Exchange, data as of 2 May 2019)

Case Study – Swire Properties



Climate-related Financial Disclosures

In 2015, the Financial Stability Board ("FSB")[29] established the Task Force on Climate-related Financial Disclosures ("TCFD") to develop voluntary, consistent climate-related financial risk disclosures for use by companies when providing information to investors, lenders, insurers, and other stak 2017, the TCFD published a set of recommendations for voluntary climate-related financial that are consistent, comparable, reliable, clear, and efficient, and which aim to provide dec information to lenders, insurers, and investors.

TCFD | TASK FOR CLIMATE- FINANCIA DISCLOSU

We recognise the risks and opportunities presented by climate change to our business. In accordance with our Climate Change Policy, we are committed to communicating our management approaches and strategies for climate mitigation, adaptation and resilience to our stakeholders. In 2018, we started to publish climate-related financial disclosures with reference to the recommendations of the TCFD under the four core categories of governance, strategy, risk management, and metrics and targets. In 2020, we completed the climate risk assessment for physical and transition risks and opportunities to our global portfolio. Our disclosures are set forth in the following pages.

Governance	Strategy	Risk Management	Metrics and Targets
SPL's Governance around climate-related risks and opportunities	Addressing the actual and potential impacts of climate-related risks and opportunities related to the Company's businesses, strategy, and financial planning	How we identify, assess and manage climate-related risks	The metrics and targets used to assess and manage relevant climate-related risks and opportunities material to SPL

Market, Reputation and Liability

Risk and Opportunity Drivers	Potential Financial Impacts
1. Increased market demand for climate resilient properties	• Increased revenue due to shift in market preference
2. Increased market demand for green and energy efficient properties	• Increased revenue due to potentially higher rental premiums for green buildings
3. Increased tenant demand for energy efficiency and data transparency	• Increased revenue due to improved tenant satisfaction and experience • Lower operating costs due to improved energy efficiency
4. Growing investor deman green and low-carbon fir investment	
5. Potential increase in insu premiums	
6. Increased exposure to re and litigation risks	

Metrics and Targets

The metrics and targets used to assess and manage relevant climate-related risks and opportunities material to SPL

The table below provides key metrics related to the impacts of GHG emissions, energy, and green building development on the financial aspects related to revenue, capital and financing, expenditures, and assets.

Financial category	Climate-related category	Metric	Unit of measure	2018	2019	2020
Revenues	Risk Adaptation and Mitigation	Proportion of total attributable gross rental income by certified green building (office and retart properties)	%	>95%	>95%	>98%
Capital and Financing	Risk Adaptation and Mitigation	Proportion of bond and loan facilities from green financing (includes green bonds, green loans and sustain-abilty-linked loans)	%	/	/	~30%
Expenditures	Risk Adaptation and Mitigation	Sustainable procurement spend	HK$	217 million	48 million	1,196 million
Expenditures	Risk Adaptation and Mitigation	Expenditures on energy efficiency / low-carbon projects supported by green bond proceeds	HK$	116 million	31 million	19 million
Expenditures	Risk Adaptation and Mitigation	Expenditures on renewable energy supported by green bond proceeds	HK$	11 million	2 million	1 million
Expenditures	Risk Adaptation and Mitigation	Expenditures on sustainable water and wastewater management supported by green bond	HK$	8 million	3 million	/

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