

Discussion for setting up JRE's Materiality

JRE-AM's CEO, Naoki Umeda had a discussion with two ESG experts and asked for their advice before finalizing JRE's Materiality.



From the left are Shin-ichi Tanabe, Naoki Umeda and Ryuichi Horie.

Profiles

Shin-ichi Tanabe



Shin-ichi Tanabe, B.Arch., M.Sc., Ph.D. is a professor at the Department of Architecture, Waseda University, Japan. He contributed to the theory of thermal comfort and indoor air quality towards to the Zero energy buildings. He is Chair of ISO/TC146/SC6 (Indoor Air). He graduated from the Department of Architecture, Waseda University in 1982. He worked as guest student at Technical University of Denmark during 1984-1986; as a visiting scholar at University of California, Berkeley and at Lawrence National Laboratory (LBNL). He was a guest Professor at the Technical University of Denmark during 2002-2003. He is a President of Architectural Institute of Japan and Council member, Science Council of Japan.

Naoki Umeda



Naoki Umeda is the CEO of Japan Real Estate Asset Management Co., Ltd. Naoki majored in city planning and graduated from the Engineering Department of the University of Tokyo in 1988. He joined Mitsubishi Estate Co., Ltd. in the same year. He is an MBA from New York University. He became Managing Director of Mitsubishi Estate London Limited in 2014. He took up his current position in 2016 and also serves as a member of the Board of Directors of the Association for Real Estate Securitization and as a councillor of the Tokyo Opera City Cultural Foundation.

Ryuichi Horie



Ryuichi Horie is the Co-founder and CEO of CSR Design Green Investment Advisory, Co., Ltd. CSR Design Green Investment Advisory, Co., Ltd. focuses on ESG advisory in the real estate and infrastructure sectors as well as research on green buildings and sustainable finance. He graduated from the University of Tokyo and holds an MBA degree from the University of California at Berkeley. Horie served as a member of global Advisory Group of UNEP FI Property Working Group and currently, he is a member of the Advisory Committee for PRI Japan Network and Co-chairperson of the Green Building Working Group at the 21st Century Financial Behavior Principles.

Umeda: Our corporate mission is to provide comfortable office environments for tenants, and to offer opportunities to invest in our outstanding office portfolio for investors. In other words, serving good to tenants leads to sustainable return for investors. As

you probably noticed, sustainable investment philosophy has been already incorporated in JRE, although global interest in ESG and sustainability has been picked up only recently. This is why we established the ESG Office in 2018 and proactively

promoted ESG initiatives ahead of our industry competitors. The ESG Office has taken the lead in enhancing disclosure, acquiring environmental certifications, and other efforts. From now on, in our second phase, I believe all our employees, not only the ESG Office, should make concerted efforts in their daily works with a keen awareness on ESG. To help make this happen, we decided to formulate key ESG issues (materiality) that are of particular importance to JRE. I feel that we need to clearly explain our future directions both internally and externally in a way that is easy to understand. I think the materiality will show the directions. I would be grateful to hear your useful opinions today.



Tanabe: In the 1980s, I studied in Denmark, which was leading the research in the indoor environmental quality field, one of my areas of specialty. At that time, I saw the tremendous efforts that were being put in to creating work environments with consideration for the well-being of employees to raise productivity, which really impressed me. Although some companies in Japan often used to invest in their factories while spending less budget on the offices at their headquarters, these attitudes are now changing rapidly in Japan. I think health and well-being, a JRE materiality, is very important and will have an impact to the society because offering comfortable workplaces with consideration for well-being will help enhance intellectual productivity.

■ Environment-Related Materiality

Horie: JRE put Climate Change Initiatives at the top of its draft list of materiality for the environment. I have the impression that, among listed J-REITs, JRE has been particularly proactive in advancing Climate Change Initiatives. Amid the global trend targeting net zero GHG emissions and the restricting of global warming to 1.5°C above pre-industrial levels by 2050, JRE is carrying out a variety of initiatives for decarbonization.

Umeda: In 2019, JRE became the first J-REIT to disclose information following the TCFD recommendations. We announced environmental KPIs in 2020, such as a 35% reduction of CO₂ emissions by 2030. Now, we have already applied for our new, more aggressive targets to be approved by the SBTi^{*1}. By advancing initiatives for achieving our new KPIs and highlighting the high green performance to tenants, we can maintain the market value of the properties and achieve higher long-term returns for investors. For example, we are accelerating the use of electricity made from renewable energy recognized by RE100^{*2} (“renewable electricity”) at our buildings. We have unveiled our policy for completing the switch to renewable electricity at our properties of 100% operational control by the end of September 2022. Completing this switch will help us to achieve our original 35% reduction target ahead of schedule, which will lead to a CO₂ reduction of more than 80%. We aim to own 5–10 zero energy buildings (ZEBs) by 2030, and we have received ZEB Ready Certification for two of our office buildings. We also became the first J-REIT to procure funds through a sustainability-linked loan.

^{*1} The SBTi is a partnership between the World Wildlife Fund, the CDP (an international non-governmental organization operating a global information disclosure system for investors, companies, cities, governments, and regions to manage their environmental impacts), the United Nations Global Compact, and the World Resources Institute. The SBTi encourages companies to set science-based targets (SBT) for GHG emissions reductions consistent with the standards required by the Paris Treaty (limiting global warming due to climate

change to well below 2°C above pre-industrial levels and pursuing efforts to limit it even further to 1.5°C).

*2 RE100 is the global corporate renewable energy initiative bringing together hundreds of large and ambitious businesses committed to 100% renewable electricity.

Horie: Introducing renewable electricity at all of JRE's properties of 100% operational control is a groundbreaking initiative, even among listed REITs. This introduction shows how ambitious JRE is about its new targets, given that it has already applied for SBTi approval. That said, how will JRE go about aiming even higher going forward?

Umeda: We would like to set higher targets following the Japanese government's carbon neutral declaration as well as the clarification at COP26 of efforts to limit global warming to 1.5°C. We also try to achieve more aggressive targets than those in the CRREM^{*3} pathways.

*3 Carbon Risk Real Estate Monitor: Sponsored by the EU, CRREM is a tool for monitoring real estate risks and showing pathways toward realizing the Paris Agreement.

Horie: GRESB^{*4} and GPIF^{*5} are also involved in CRREM, which is rapidly becoming the standard as an initiative for quantifying transition risks in real estate. The fact that you expect to achieve reduction targets that exceed the CRREM pathways is simply groundbreaking. Professor Tanabe, how do you think moves for net zero emissions by 2050 will affect the real estate industry and what expectations do you have of JRE in this context?

*4 GRESB measures the environmental, social, and governance-related (ESG-related) performance of individual companies and investment funds in the real estate sector. It is used as a tool for selecting investees and during dialogue with investees.

*5 Government Pension Investment Fund

Tanabe: COP26 demonstrated that initiatives over

the next 10 years will be crucial. The same applies to initiatives in the real estate industry. For example, 70% of total CO₂ emissions in Tokyo are accounted for by buildings and housing. Some of these are large buildings in central Tokyo that see intellectual production activities. Reducing the emissions of such buildings to net zero while maintaining productivity will require ingenuity. As an example, properties in the UK with low energy-efficiency ratings cannot be leased and a measure prohibiting the leasing of properties with an intermediate rating from 2030 has been announced. Only 20% of properties on the market have the high ratings needed to make them leasable at this moment. I expect to see the same situation in Tokyo soon. JRE is looking ahead to the future when there is a clear division between buildings that are of tenants' choice and buildings that are not.

Horie: I note that JRE has set Environmental Consideration of Portfolio as one of its materiality items and made acquiring environmental certifications a KPI. This is a perfect example of an initiative where JRE can be chosen by tenants thanks to environmental performance.



Umeda: Exactly. We will continue acquiring environmental certifications as that also gives us incentive to promote decarbonization. More importantly, those certifications are useful to appeal to tenants. Recently, tenants have become more aware of ESG in their own businesses than you might previously thought. In terms of many tenants'

business strategy, it is inevitable for those companies that are keenly aware of ESG factors to choose office buildings with a high level of environmental performance and buildings that promote the health and well-being of their employees. It will be nice to acquire certifications and show the strong environmental performance of our buildings in a way that is easy to understand for tenants.

■ Social Materiality

Horie: In a recent survey, 90% of people believed that health and well-being had become more important because of the COVID-19 pandemic. Also, a study showed rent premium of between 4 and 7% for properties with health and well-being certifications. Tenant Engagement comes first in JRE's list of social materiality. From the perspective of health and well-being, what do you see as offices of tenants' choice?

Umeda: Offices where employees can work comfortably and with peace of mind are extremely important. For example, we aim to be more competitive by thoroughly addressing tenant requirements such as non-contact features, good ventilation, and other measures in common areas. This will lead to returns for investors in the long run. But I think health and well-being are hard to visualize numerically, unlike the environment.

Horie: I agree. Since it is difficult to visualize health and well-being, acquiring certifications will be the key to differentiating JRE's buildings from others.

Tanabe: Comparing internationally, the health and well-being aspects of buildings in Japan are at an exceptionally high level due to the regulations in the Act on Maintenance of Sanitation in Buildings. However, the COVID-19 pandemic has changed the role of the workplace. The meaning of health and well-being has been changing in such areas as non-contact features, ventilation, acoustic features,

communication, and consideration for diversity. Offering spaces tailored to new needs, especially in common areas, and acquiring certifications will be key themes, as Mr. Horie pointed out. For example, recently in the United States, where visualizing the rating of buildings is also important, the WELL Building Standard, has been created. This is the world's first certification system focusing on people and health.

Horie: As for Employee Initiatives, Human Resources Development and Diversity Promotion and Health and Well-being are indicators ESG evaluations emphasize. These evaluations pay close attention to the ratio of female senior management and female directors. For social and governance aspects, JRE seeks to ensure the diversity of its employees and of its Board of Directors and has established the female director ratio as a KPI.

Umeda: When I returned to Japan after spending many years in London, I felt diversity was not working adequately on many fronts. That's why, I set about making improvements, such as recruiting female and non-Japanese people, and encouraging communication by introducing a free address seating free drink in our comfortable cafe area, and other innovations. Although we have a slightly higher ratio of female to male employees, the number of female senior management is still low and overseas observers may feel that faster action is required. Even so, as there is momentum in Japan as a whole for making substantial changes to society, I believe the diversity of our workforce will look very different in five to 10 years' time.

Tanabe: The social advancement of women and their degree of freedom in society is rather behind in Japan. I worked at a women's university for a decade. Coming into contact with young people, I know that their capabilities and enthusiasm is the same, regardless of gender and I am sure that Japan will

change going forward. Personally speaking, I thought that the real estate industry was male dominated so I was surprised to learn that JRE-AM's workforce has a roughly even gender balance.



■ Governance-Related Materiality

Horie: Enhancing governance systems at both JRE and JRE-AM has attracted considerable attention from investors. The implementation of training and internal audits, on conflicts of interest as well as human rights and business ethics (preventing fraud, corruption, and other practices) has also been assessed in ESG evaluations. JRE aims to promote dialogue through disclosure as a way to engage with stakeholders and maintain and improve its ESG ratings. JRE also began publishing a sustainability report in 2020 and is working proactively on its ESG ratings. In the past year, we have seen a series of moves to make the disclosure of ESG information such as TCFD mandatory, by the Tokyo Stock Exchange and in securities reports.

Umeda: I regard disclosure and dialogue with the stakeholders as my most important role as CEO. We will keep our communication actively to meet the expectations of many stakeholders. A few years ago, I sometimes questioned myself why we did not receive more positive evaluations from ESG rating agencies though we worked hard on ESG issues. But now I realize, as some of ESG evaluation institutions mainly base their evaluations on disclosed information, a favorable evaluation will not be

forthcoming if information disclosure is not enough. I think it is sound management to thoroughly disclose our initiatives and accept input on areas where we are lacking.

Tanabe: J-REITs disclose such figures as utility costs for building, helping to provide an extremely high level of transparency. With J-REITs making such efforts, lobbying local governments to facilitate comparisons of actual energy and GHG emissions figures for each building would encourage companies to compete with each other to achieve the best figures. Such competition would promote ESG information disclosure throughout society and synergistically provide a boost for J-REITs as a whole.

■ In Closing

Horie: Today's discussion has given me a clear understanding of President Umeda's approach to ESG matters, which is that they are a means to offer value to society and investors by offering properties of tenants' choice, rather than an end in themselves.

Tanabe: I agree. Offering places where those working at JRE buildings can work comfortably and in good health, and at the same time giving sustainable return to investors by investing in those buildings is very fundamental philosophy. I think that is in line with the very essence of the ESG concept.

Umeda: JRE has a responsibility to investors to continuously pursue sustainable return by forward-thinking and proactive asset management. With an eye on business environment changes, including aging and declining population in Japan, rapid advance of IT and the global pandemic, we will unwaveringly continue offering offices of tenants' choice. If our actions contribute to ESG matters and benefit society, nothing would please me more. Although our efforts may take time to produce

results, we are eager to consistently meet the expectations of investors, tenants, and other stakeholders through our materiality initiatives. Let

me end by thanking you both for the insights today.

