

Green Building Series: Part 5



In today's tough real estate market many building owners are struggling with costs and finding ways to attract new tenants. Going "Green" continues to be the most popular option for building owners, even with the upfront costs of doing so. The article below is proof that building owners are willing to spend the money to attract better clientele even in the down economy. Details are below:

Green Premium Continues to Justify Implementation Costs for Building Owners

Joint CoStar and USGBC Presentation Finds Sustainable Building Efforts are Expanding Despite the Recession, Though Owners are Less Certain About Recouping Their Green Investments



By Randy Drummer
Credit: CoStar Group

The economic payback for building owners from 'going green' has been tested in the crucible of the worst economy since the Great Depression, and while the premiums in rental rates, faster lease-up times and lower vacancy associated with green buildings varies market to market, the corresponding increases in rental income, together with the resulting energy savings in operating the property, continue to justify the modest additional costs associated with going green in most markets.

For tenants, a growing body of research continues to show that buildings with better air quality, natural lighting and variable temperature control yield greater productivity by employees. Also, separate metering and individual utility billing of tenants for their energy use encourages conservation and additional cost savings. Those are some of the main conclusions taken from "Current Trends in Green Real Estate," the second webinar presented jointly by CoStar Group, Inc. and the U.S. Green Building Council (USGBC).

In taking stock of the current green building market, the USGBC found that overall LEED certification activity has remained relatively stable during the turbulent economy, as measured by total square feet certified by the USGBC for all of the 10 Leadership in Energy and Design (LEED) rating systems, including certifications of existing buildings, core-and-shell and new construction. According to presenter Chris Pyke, USGBC vice president of research, the leading green building organization has certified more than 26 million gross square feet of additional space (among all categories and property types) for LEED each month on average over the last few quarters.

One big change, however, has been the market shift in LEED certifications from new development. Today, much of the USGBC's certification activity has shifted to LEED for Existing Buildings (LEED-EB), which has seen certifications jump sharply from less than 15% of all certifications in early 2008 to more than 35% in second-quarter 2010, Pyke said. At the same time, the proportion of LEED for New Construction (LEED-NC) awards has fallen from nearly 60% of all certifications in late 2008 to about 30% at midyear 2010.

"The top-level story we see is the overall stability in the relative number of square feet coming through the green building process, which has continued to grow over the last three years, but with a pretty sizable shift from new construction to existing building [certifications]," Pyke said.

Credits for water reduction and energy efficiency have jumped from 70% of new construction projects to over 80% over the last three years. However, points for formal review of building design and plans and ongoing monitoring by a third-party commissioning authority, called enhanced commissioning for LEED-NC, has fallen since 2007, said Anthony Guma, USGBC manager of real estate research, who also participated in the presentation.

LEED operations and maintenance credits for existing buildings have remained stable, although commissioning of existing buildings has also declined since 2008 as building operating budgets have become more constrained, Guma said.

Still Green To Be Made in Going Green

Updating the initial analysis CoStar did in its "Does Green Pay Off?" study, CoStar Vice President of Analytics Norm Miller found that LEED-certified office buildings command a \$2.05 per square foot rental premium over all office buildings (multi-tenant, built since 1995.)

However, in the current cost-conscious economy, tenants and building owners have become less certain of expected returns on green investment. Whereas prior to the recession, LEED-certified buildings enjoyed noticeably faster lease-up times and lower vacancy rates in addition to commanding higher rental premiums compared with their non-green peers, vacancy rates have remained relatively high for Class A LEED-certified buildings, with a national average of 37.6% compared with 25.8% for all Class A office.

Miller, a leading authority on green building economics, noted that the higher average vacancy rate in LEED office buildings reflects two important factors. The first is that a significant number of the new Class A office buildings that started development before the recession and came online after the economy had begun to weaken were LEED certified buildings. As a result of the economy, many new office buildings have struggled to attract tenants and have higher than average vacancy rates.

To illustrate this point, Miller analyzed two sets of office buildings, those built before the recession (completed 2000-2005), and those constructed since 2005. Class A LEED office buildings that completed construction before the recession hold a significant advantage over the national average for all Class A office buildings, with the LEED buildings averaging \$28.50 per square foot in rent with an average vacancy rate of 6.5%, compared with \$25.89 per square foot in average rent and an average vacancy of 10.7% for all Class A office stock.

Then analyzing Class A office buildings completed since 2005, the LEED certified buildings continue to attract higher rents, with an average of \$33.24 per square foot compared to \$30.11 per square foot for all Class A office. But the national vacancy rate for all Class A LEED office properties was 36.4% at the end of the first quarter of 2010, compared with 31.1% for all Class A multi-tenant office property.

"We do find that it does continue to pay to go green," Miller said. "In the long run buildings that do not include sustainable features run the very real risk of becoming obsolete. And it will likely be very risky to own buildings that do not have sustainable features in the future."

"We also know that tenants in green buildings enjoy higher levels of productivity and see a real benefit and value to having their employees in green buildings. Because there are still so few green buildings out there many tenants haven't experienced that impact yet. But we believe this will change in time as those markets become more educated and tenants begin to pursue the productivity benefits of green buildings," Miller said. "We expect rental premiums or energy savings to more than justify the added costs for energy saving green features like separate meters, motion detection light devices, or water savings devices."

