

Building a sustainable future

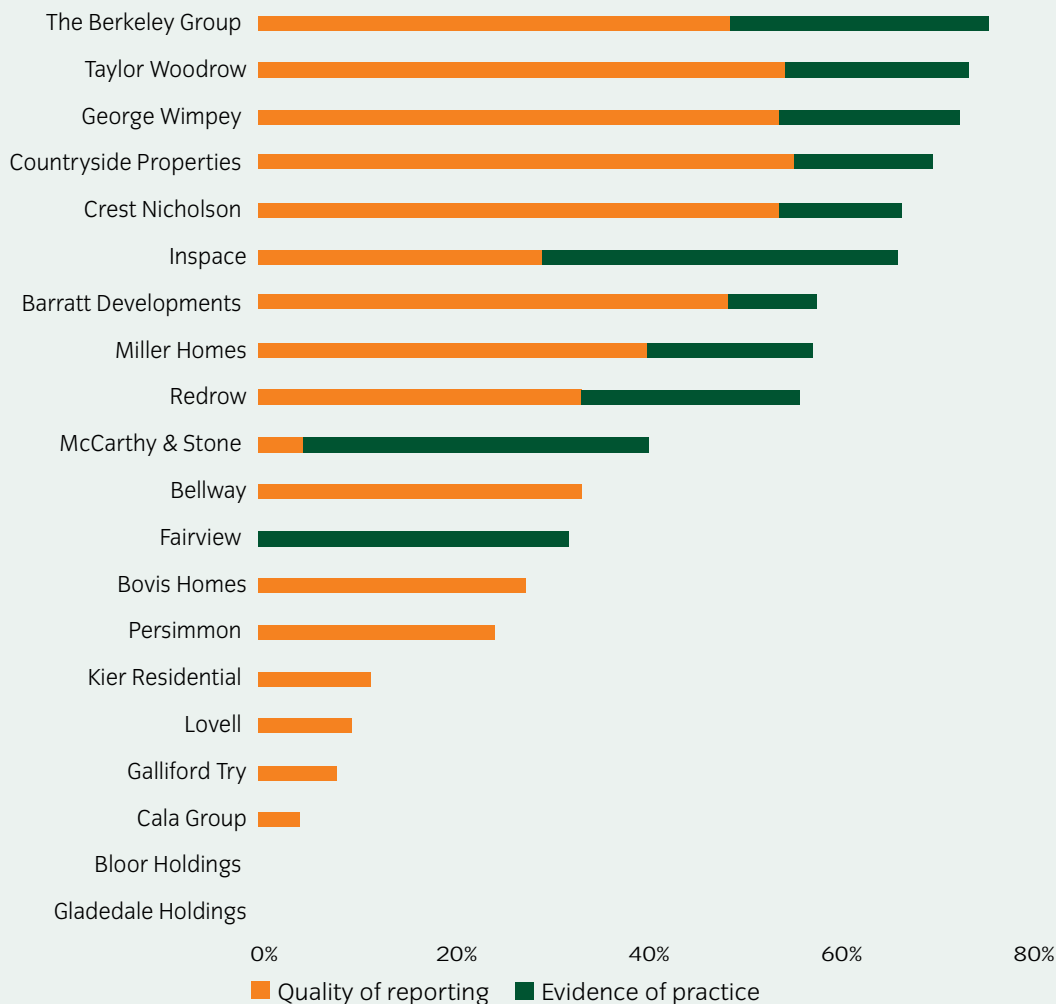
In October, NextGeneration published an analysis of the performance on sustainability of the UK's Top 20 home builders, both listed and unlisted, responsible for delivering over 95,000 homes each year.

As Figure 1 indicates, three leading companies emerge from the benchmark – The Berkeley Group,

Taylor Woodrow and George Wimpey (now merged to form Taylor Wimpey).

The report, entitled, 'Building a Sustainable Future: UK home builders' progress in addressing sustainability is available at: http://www.insightinvestment.com/global/documents/riliterature/367922/nextgen_benchmark_report

Figure 1: Top 20 housebuilders' overall performance



Background

The imperative to address sustainability issues in the housing sector has never been stronger. The acute shortage of housing, especially affordable housing, combined with issues of land availability and the recognition of the urgent need to address climate change, has made building sustainable homes and communities one of the Government's key priorities. Sustainability can no longer be treated as a fringe issue by the home building industry. The current debates about the provision of sufficient land, the effectiveness of the planning system, the structure of the home building industry and market demand are all inextricably linked to the delivery of sustainable homes and communities.

To respond to this challenge, the NextGeneration initiative (see Box A) brings together many of the UK's top home builders with three key stakeholders: Insight Investment, along with WWF-UK and The Housing Corporation.

Methodology

The benchmarking was undertaken in two phases:

Phase one: The top 20 companies' publicly available information (corporate responsibility reports, annual reports and accounts, corporate websites) was assessed in three categories: strategy, governance and risk management, impact on the environment and impact on society. All companies were awarded a score to reflect the quality of their reporting.

Phase two: NextGeneration members (11 companies) provided a more detailed picture and qualitative evidence of their practice on sustainability through meetings and intensive engagement with Upstream. These companies were awarded a second score to reflect their practice.

A score of 100% in either phase would not indicate that a company was 'completely sustainable', rather that it had achieved best practice in the industry, as defined by the NextGeneration criteria.

Box A: NextGeneration

Previous to this year's NextGeneration benchmark, Insight Investment and WWF-UK jointly benchmarked the performance of the UK's major publicly listed home builders on sustainability practice and reporting in 2004 (13 listed companies) and 2005 (12 listed companies).

NextGeneration was launched to build on the success of these benchmarking exercises and to expand their reach and ownership. Set up as a multi-stakeholder initiative, NextGeneration aims to drive best practice on sustainability into the heart of the housing sector by encouraging the industry itself to embrace more sustainable house designs and delivery. It is intended to be a platform through which developers can both identify the sustainability-related risks they face, as well as develop a good understanding of how best to take advantage of the related opportunities.

NextGeneration is supported and directed by The Housing Corporation, WWF-UK and Insight, all of which sit on its Executive Committee. Upstream acts as a secretariat to the initiative, carrying out the analysis for the benchmarking and delivering a range of services to NextGeneration members. In addition, a Steering Group with representatives from the Executive Committee and member companies helps to guide the evolution of the initiative and ensure good governance.

The first output of NextGeneration is this, the 2007 benchmark of the UK's top 20 home builders based on the number of units built during the last financial year (2005/06). The benchmark incorporates two sets of scores: the first that rates the quality of reporting of the sector on sustainability and the second that rates its performance in this area.

NextGeneration plans to repeat this benchmark every two years and in alternate years produce a benchmark that focuses on builders' performance on a specific issue. In 2008, the issue will be climate change.

Overall results

The results are broadly encouraging: they indicate that a number of companies in the sector have recognised the pivotal importance of sustainability issues to their business operations and are responding strongly. However, they also highlight the large gap between where the industry is now and where it needs to be if it is to achieve the Government's 2016 vision of all new homes being zero-carbon.

The Housing Green Paper, the Code for Sustainable Homes, the Building a Greener Future policy document and the Draft Strategy for Sustainable Construction together lay out the Government's vision for achieving zero-carbon homes by 2016 and set out a demanding agenda and set of standards for home builders.

It is clear from in-depth discussions with the NextGeneration corporate members that they are struggling to keep up with the very rapid pace of change in this area and have yet to fully grasp the implications of sustainability for their businesses:

60%	of home builders recognise climate change as a significant issue to the sector but none has a climate change policy in place;
25%	have an understanding of the carbon footprint of their operations;
15%	of companies have sustainable procurement policies;
70%	of home builders report publicly on their approach to sustainability;
65%	have published a corporate sustainability policy;
65%	have waste management strategies in place; and
60%	have set targets to improve the energy efficiency of their homes.

The results showed significant variety in the performance of the top 20 home builders with scores ranging from 74.6% to 0%, and a sector average score of 38.8%. NextGeneration members outperformed non-members with average scores of 59.8% and 13.1% respectively. This is not surprising, given that members were able to provide additional non-public information to support their scoring.

Listed home builders (49.0%) also performed better on average compared with the private companies (28.7%). Six companies do not fully disclose their approach to sustainability in their corporate reporting or websites, and are also not NextGeneration members:

Kier Residential, Lovell, Galliford Try, Cala Group, Bloor Holdings and Gladedale Holdings. Their ranking as the bottom six companies does not necessarily reflect their sustainability performance, but rather reveals their lack of disclosure in this area. As with any company not currently a member of NextGeneration, we encourage these developers to join their peers and engage with the initiative to showcase their approach to sustainability and performance in this area.

Strategy, governance and risk management

Companies achieved an average score of 50.5% in this section, reflecting the fact that a number of companies now have well-developed and implemented strategies in place across their businesses.

But while 60% of all companies have identified the key sustainability risks faced by their business, only 35% have begun to assess the commercial implications of these risks. This means that few companies are in a position to assess how sustainability adds value to their businesses. Examples of such benefits include:

- Cost savings related to good waste management: Taylor Woodrow, one of four companies to score 100% for construction waste management, disclosed in its 2006 report that the cost of disposing of construction waste had decreased to £291 from £351 per home in 2005, despite increasing landfill tax;
- Health and safety (H&S) insurance savings: one company reported an annual saving of £1 million in its insurance costs due to making improvements in its H&S systems;
- Gaining planning permission: The Berkeley Group disclosed in its 2006 Sustainability Report that it believes that full stakeholder engagement in the planning process at its Kingsway Square development meant it only took 13 weeks to obtain detailed planning permission for the project (including Section 106 agreements), listed build consent and conservation area consent.

These commercial benefits are rarely aggregated and articulated by companies to their investors or others – something that all companies should seek to do.

As many as 70% of the companies now produce a separate sustainability report and/or use websites through which they disclose their approach to sustainability and the scope and breadth of sustainability reporting has significantly improved in recent years. However, areas in which companies transparent could be improved are risk management, target setting and performance data. This would enable stakeholders to develop a clearer view of their

approaches to sustainability and their plans for the future. It would also increase the level of sophistication of their reporting, bringing it closer to the quality and completeness seen in other sectors.

While 60% of home builders recognise climate change as a significant issue to the sector, none has a climate change policy in place.

Impact on the environment

Companies scored most poorly on their approach to addressing their environmental impacts of all three aspects of the benchmark, scoring 31.6% on average. This is particularly worrying as environmental issues are at the heart of the Government's policy agenda – notably climate change, energy, water and waste.

It would seem reasonable to expect that climate change – as arguably the most serious risk facing the housing sector today, and the key sustainability issue in the public consciousness – would be at the top of the sustainability agenda for home builders. However, analysis of the sector reveals that developers are not yet giving sufficient strategic weight to the key risk of climate change. While 60% of home builders say they recognise climate change as a significant issue for the sector, none of them currently has a climate change policy in place. Failing to address this issue at a strategic level means that companies cannot have a full understanding of the commercial implications – both the risks and opportunities – that climate change poses to their business operations.

Some of the key risks include:

- Flooding risk (particularly important concerning land acquisition strategies and land banks);
- Adaptability of homes being built for a changing climate;
- The embodied energy in building materials; and
- The energy performance of dwellings.

In addition to the introduction of Energy Performance Certificates, climate change issues feature strongly in the forthcoming Code for Sustainable Homes; developers need to accelerate their efforts to prepare for, and comply with, these new legislative and regulatory drivers.

The industry also has some more technical and practical challenges to address, such as:

- How will renewable energy requirements be delivered in the face of technological and cost uncertainties? Crest Nicholson provided the only example of a zero-carbon development under construction.

- How will considerable reductions in water consumption be achieved and still provide homes that are appealing in the market place? Only 30% of home builders are currently measuring the performance of their dwellings in terms of water consumption.
- How do homes need to be designed to adapt to climate change?
- Stepping up to waste legislation.

Waste management is an area where home builders have clearly recognised the business benefits of a proactive approach and have responded accordingly. With the challenge of impending legislation, 70% of home builders provided evidence of waste management being undertaken on sites, with 50% of companies providing performance data in relation to waste across all sites. However, even in the highest-performing environment criteria, some builders were unable to show that they were fully prepared for the site waste management plan legislation which comes into effect in 2007.

Impact on society

The 20 companies benchmarked scored 43% on average for their efforts to address their impacts on society. In much of the current dialogue on sustainability matters, socio-economic issues are a poor relative, rarely considered beyond the rhetoric of 'building sustainable communities'. Moreover, these issues are not well covered by the Code for Sustainable Homes, which sends the signal to developers that they are less important. But the socio-economic dimensions of sustainability are the 'glue' that holds communities together.

The sector clearly takes H&S seriously. Many of the top 20 home builders are providing evidence of implementing robust H&S policies and management systems with 70% publicly reporting their RIDDOR rate (Reporting of Injuries, Diseases and Dangerous Occurrences Regulations). However, fatalities have increased recently in the construction industry, indicating that home builders must continue to work hard to drive down incidents and accidents. Two important steps would be for the industry to develop and adopt a standard RIDDOR measurement system and for companies to externally audit their H&S performance to ensure that the data disclosed is accurate.

Both the Housing Green Paper and the Draft Strategy for Sustainable Construction highlight concern over the lack of skills among the construction workforce needed to deliver sustainable communities on the ground. The NextGeneration benchmark has shown

that even when home builders have well-developed sustainability strategies, the sector's skills shortage is one of the contributory factor to not delivering fully on that strategy.

While 65% of home builders were able to provide examples of improving community wellbeing through various initiatives, only two companies provided evidence of achieving the Lifetime Homes standards across all developments – standards relating to a home's accessibility and flexibility. While this finding highlights the need to address design issues in terms of demographic changes, as noted above, it also appears that the sector has not yet begun to think about whether current design techniques can deliver housing stock capable of being adapted to future climate changes.

The future

The Government has committed to building many more homes each year than it has in the past, to ease a general housing shortage and particularly the dearth of key worker and affordable homes. This offers the prospect of growing revenues for the sector. But at the same time, the Government has said that the industry must deliver sustainable homes to contribute to the 60% decrease in greenhouse gas emissions the UK needs to achieve by 2050 – and which will be embedded in law when the Climate Change Bill is passed in 2008. This challenge only becomes more pertinent in light of WWF-UK and other organisations calling for the Government to increase this target to 80%.

Overall, it appears that both Government and the industry have focused on a few aspects of sustainability to the detriment of others, i.e. treating the interconnected aspects as if they can be de-linked and delivered in a piecemeal fashion, or that certain elements can just be ignored as they are less important. The reality is that sustainability is a multi-dimensional concept and has to be delivered as a package.

In terms of home buyers' views, several recent surveys have found that most home buyers do care about environmental issues, particularly climate change, and they would like (and indeed expect) a new home to be energy efficient.

Companies that can capitalise on the building boom and find the most cost-effective ways of building sustainable homes today will be tomorrow's winners. Critical to success will be investment in innovation and a willingness to break from the past to design and deliver homes that are both efficient and adaptable to the changing but uncertain future climate.

Recommendations

We therefore make the following recommendations to both industry and Government in the hope that home builders will be able to rise to the challenges of delivering sustainable communities and the Government will provide the necessary support to help the sector achieve this.

Recommendations to the industry:

- Seek to understand and better articulate the commercial implications – both risks and opportunities – of the sustainability issues facing the sector.
- Seek to understand the commercial value of sustainability to core business operations and include commentary on this in financial presentations.
- Develop a strategic approach to climate change by introducing corporate policies and setting short- and long-term targets aligned to the Government's targets to reduce carbon emissions of both operations and product.
- Innovate and experiment to understand the commercial, technical and customer implications of building homes to the levels in the Code for Sustainable Homes and share best practice publicly.
- Translate the best practice exhibited occasionally on a few developments into standard practice across all developments.
- Implement a communications strategy to address how sustainable housing can be better marketed to the customer and to promote more sustainable lifestyles among occupiers.
- Think holistically about operations to ensure that cost savings in sustainable materials specification and construction waste management are captured by the entire businesses.

Recommendations to the Government:

- Ensure that the recent plethora of policy documents and legislation provides clear guidance for home builders in terms of achieving the 2016 zero-carbon housing target; indeed, provide a consistent definition of 'zero-carbon'.
- Ensure that future iterations (for example, the proposed review in 2010) of the Code for Sustainable Homes are holistic in their approach to addressing sustainability issues.
- Ensure the Code for Sustainable Homes is consistent with standards being set in other policy documents and legislation.
- Introduce incentives/sanctions to encourage home builders in building more sustainable housing.

- Ensure fiscal measures are in place to help home builders realise the commercial benefits of building sustainable housing – notably through stamp duty exemption and council tax reductions.
- Take a leading role in marketing sustainable homes to the house buying market.

We hope the findings of this process will enable home builders to identify the key challenges and opportunities, respond to these with clarity and assist the Government in understanding the very practical barriers that the sector has to overcome.

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Produced by the Insight Investor Responsibility Team

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