

Asset Backed Inheritance Tax Service’s Sustainability Spotlight

We are delighted to present the second edition of the Stellar Sustainability Spotlight. This edition will showcase the steps taken to bolster internal processes and drive sustainability within The Stellar ITS, Stellar Growth IHT Service, Stellar Bespoke IHT Service and Stellar Business IHT Service (the “AB Services”).

Why?

We recognise the importance of our position as stewards of clients’ capital. As owners of each business within our AB Services, we also recognise that we have both the direct opportunity and responsibility to drive improvements for the betterment of the environment and wider stakeholders without compromising potential returns.

Our AB Services commit capital to businesses across a breadth of sectors, all of which are underpinned by tangible assets. According to the Chartered Institute of Building, approximately 40% of carbon emissions derive from the construction, operation, or maintenance of buildings. As this encapsulates the key activity undertaken across businesses within our AB Services, we are striving for improved measurement of negative impacts and to enhance practices that will have a positive effect on the environment and society.

Our activity aligns with the general direction of travel that is notable across UK real estate. A recent report by Knight Frank notes that three-quarters of surveyed investors have minimum environmental certification criteria for new acquisitions. Knight Frank note that the due diligence process for new acquisitions is becoming increasingly detailed and ESG factors are at the forefront. As long-term investors, we feel ESG is an inevitable structural shift in the UK real estate landscape that is already underway. There is therefore further incentive for us to incorporate ESG and sustainability practices into our investment process as not doing so could reduce acquisition opportunities and result in our assets being filtered out by ESG conscious purchasers when we come to sell. By enhancing the focus on sustainability today, we will be best placed to thrive in the medium and longer-term.

How?

Unfortunately, there is no one size fits all approach to ESG assessment. The guidance from regulators is inconsistent and often open to interpretation.

This is further compounded by ESG rating agencies using quite different methodologies, leading to often contradictory outcomes, where the same company can be deemed “good” or “bad” depending on how the rating agency weights each of the E, S, and G.

When designing our ESG approach we were clear that it had to be simple, flexible, and pragmatic. Quantitative data is important, but so are the more intangible qualitative elements.

Each of our asset backed businesses are scored out of a total of 40 points, with 10 points on offer for each of the E, S, G, as well as their direction of travel (DOT). The scoring is subjective and material factors across the different sectors we operate can vary. We have established bespoke questionnaires for each sector which aim to get to the heart of what good practice looks like across each respective industry. Businesses are required to maintain a score of at least 24. As we own each business, divestment is not our first port of call. If a business is tracking behind expectations, it will be subject to enhanced scrutiny with progress against performance plans monitored at our monthly investment committee meetings.

Our first full round of scoring was completed as at the end of December 2023.



Implementation

We underpin our assessments with established benchmarks, including the UN Sustainable Development Goals. As owners of the businesses within our AB Services, we can drive positive impact directly. We do this by engaging with each of the counterparties that we work with across these businesses (typically, developers, operating partners, or management teams) to ensure that all parties are aligned driving the improvements contained in the action plans that we establish.

“To improve is to change; to be perfect is to change often”

Tunbridge Wells Development

This is a development of five light industrial warehouse units in Tunbridge Wells, Kent.



The real estate sector has several benchmarks against which developments can be independently assessed and graded, ultimately highlighting that the development has positive ESG credentials and is therefore more attractive to occupiers or investors and potentially has a higher value than if uncertified. For commercial real estate buildings, BREAAAM certification has become established as the go-to assessment tool. As noted earlier in this spotlight, Knight Frank recently reported that 47% of buyers look for properties with BREAAAM ratings of ‘Excellent’ or ‘Outstanding’.

This development is being built to a BREAAAM certification of ‘Excellent’ which is the highest feasible certification achievable for light industrial units of this type. Achieving this rating provides a measurable way of ensuring all parties are focused on developing units that will operate sustainably post-build. As well as enhancing the sustainability credentials of this project, building the units to this standard also ensures that we will have the opportunity to sell the units to a broad range of buyers once built many of which will have an ‘Excellent’ BREAAAM rating as a core feature of their acquisition criteria. There are improvements to be made in terms of quantifying the impact on the environment of the build process itself. Incorporating better measurement and mitigation of these emissions is a key focus for the investment team in 2024.

The development is being managed in accordance with all appropriate standards of health and safety and labour conditions.

Post completion, the development will also have a positive socioeconomic impact on the area as it will provide new light industrial units that will be utilised by local and national businesses. This will create new jobs and have a positive impact on the economy.



From a governance perspective, there are multiple layers of oversight across each core function of the development. Each key role is being carried out by parties with well-established track records and each has independent third-party oversight. As with all our development projects, the deal is structured to ensure that investors benefit from a priority return. This is a key risk mitigant. The majority of our development partner’s remuneration is contingent on the profit ringfenced by our investor’s priority return being exceeded, which means interests are aligned and our development partner is incentivised to ensure that all core risks are controlled (expenditure, time delay and the sales process). Equity is also committed to the project at outset by our development partner.



David Stein, Investment Manager

Having joined Stellar in 2019, David has spent the past five years acquiring expertise managing assets within the AB Services through the entire deal cycle.

David is a passionate advocate of asset backed investing and a CAIA charter holder.

To support Stellar on its quest to integrate ESG and sustainability best practice into its investment management, David also attained the CFA Certificate in ESG Investing.

Important Information

Your capital is at risk and may not get back the full amount invested. Investments in smaller companies will normally involve greater risk or volatility than investments in larger, more established companies. Tax treatment depends on the individual circumstances of each Investor and may be subject to change. This document is dated **April 2024** and is intended for retail investors and their advisers and has been issued by Stellar Asset Management Limited (‘Stellar’). This document is for information purposes only and does not form part of a direct offer or invitation to purchase, subscribe for or dispose of securities and no reliance should be placed on it. You should only invest based on the relevant Product Literature available from Stellar and your attention is drawn to the charges and risk factors contained therein. Stellar does not provide investment or tax advice or make recommendations regarding investments. Stellar of 20 Chapel Street, Liverpool, L3 9AG is authorised and regulated by the Financial Conduct Authority.