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ROI of sustainability

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In past columns we have discussed sustainability, green building materials and global warming. But are we really talking about real estate and is there a connection?

Portions of this seemingly unstoppable movement are deeply rooted in the concern for the environment and the science-based proof of the impact that greenhouse-gas emissions have on the quality of life of all beings on the planet.

This has created two extreme camps: Camp 1 has deeply held beliefs about environmental degradation and the impacts added to that degradation by humans.

Camp 2 has equally held beliefs that the concerns are rooted with inaccurate science. For a moment, let's pull out of the equation the emotionally charged belief that humans are adding to global warming or that the science is wrong.

Clearly, even without these components, we see that the climate is changing. It is with this baseline proof that we need to look at the real estate industry business model and develop strategies to take advantage of this new addition to the equation.

The new global economy, especially with the emergence of Chindia (China and India) and Dubai, has massive influences on land use and real estate. Energy, efficiency and cost are the components that will play an increasing role in the return on investment or ROI.

The era of readily available and cheap energy is over. We now know we have a finite amount of fossil fuel. Most energy experts suggest that even if we tap the vast Alaskan and Gulf of Mexico oil reserves our current rate of global usage will deplete these resources in the next 50-100 years. Even if we go a step further and find innovative methods to extract oil from oil shale, it is still a finite resource. Experts also suggest that the oil production peaked in the past few years, meaning that we have entered the era when the amount of oil that can be economically extracted will decline. The average consumer feels this most harshly when filling up at the pump. However, similar cost pressure affects heating oil, the electricity that powers our air conditioners and lights, the cost of our food, air travel and the hundreds of thousands of products that contain petroleum as their base. It is clear that none of these items are getting any cheaper.

As land use and real estate leaders, we need to decide if we are victims or leaders. We will not solve our two-century-old focus on fossil fuels overnight, but we stand at a crossroads of economic competitiveness and energy leadership. For example, Toyota, which has led the world in the production of hybrid vehicles, has a market capitalization more than five times greater than Ford and GM combined. The reason is fairly simple; they are leading the world in solving transportation needs in concert the energy efficiency. Another leader is the Texas oil and gas entrepreneur Boone Pickens, who is making a $2 billion investment in wind energy. In a recent article in *Fast Company*, Mr. Pickens stated with gusto that his decision to go green is not as much about the environment but rather about the ROI. Reliance on foreign-controlled sources of energy will not only get more costly, but also become far more challenging in a global environment where we must compete for shrinking resources. Wind is renewable, domestic, and poses little environmental risk.

We can see examples of how this is affecting real estate and land use locally and as individual developers, investors and property owners. The renewable energy opportunity of Imperial County, which has been identified as one of the leading locations in our nation for the development of wind and solar power, is driving great opposition to the Sunrise Power Link. Looking at the individual building or at the asset level, we see that energy and operating costs are on the rise. The higher the operating costs the lower the ROI, which lowers the value of the asset. This indicator alone builds the case for putting sustainable energy and building efficiency into place. When evaluating any income-producing property from here on out, tenants want to limit their occupancy cost (including utilities) and have a steady and predictable cost structure. Landlords seek the same metrics. If building operating costs were to see the price spikes we see at the gas pump our battered real estate industry would be in far worse shape. While utility rates have not spiked yet, it is not likely they will decline.

LEED standards are one popular metric to judge and control energy usage. However, within five years, LEED will

be standard in municipal building codes. In terms of new development, it is already becoming clear that space that does not meet LEED standards is simply less economically competitive. The issue is not what energy-efficient "brand" one stamps on a building. Rather, it is what systems can be built into new building, what forms of urban design and land-use planning can be instituted, to limit or even decrease the amount of energy they use. Reducing usage and thus reducing cost simply flows to the bottom line. We have entered an era when our sustainability decisions are no longer a strictly emotional or environmental issue; they are clearly an economic issue.

On June 26, at the Balboa Theatre, ULI San Diego/Tijuana will be presenting awards to 15 outstanding smart-growth projects, plans and people. Smart growth is defined as economically feasible, environmentally sound and equitable to the community at large. Smart-growth principles are becoming a necessity of the ROI equation. Please join us to celebrate San Diego's award-winning smart-growth winners and to get ideas for how to increase the return on your real estate investments. For tickets, go to ulisd.org.

Pauker is chair and Lydon is executive director of Urban Land Institute of San Diego/Tijuana.