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Long Lease Property Fund

Considering climate risks

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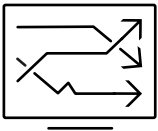
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Introduction

As abrdn's largest real estate fund, we continue to improve our management and assessment of ESG (environmental, social and governance) risks and opportunities. One of our key priorities is on developing our strategy to move the fund to a net-zero position and further integrate assessment of climate risks and opportunities.

According to the Taskforce for Climate-related Financial Disclosures (TCFD), climate risks are categorised as follows:



Transition risks are those that relate to an asset's ability to decarbonise. An asset can be exposed to risks as a result of carbon pricing, regulation, shifts in technology, and demand related to the transition.



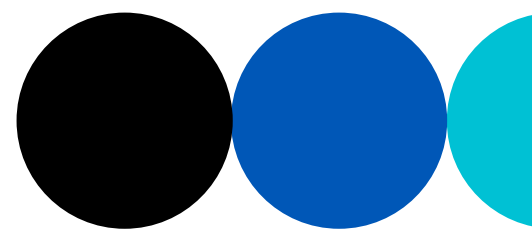
Physical risks are those that relate to an asset's vulnerability to factors such as increasing temperatures and extreme weather events as a result of climate change. Exposure to physical risks may result in, for example, direct damage to assets, rising insurance costs or supply chain disruption. We must also consider the costs of adaptation (i.e. the infrastructure required to protect from physical damage).

Climate risks, alongside wider ESG risks and opportunities, are integrated as standard throughout the abrdn real estate investment process from acquisition, refurbishment and development and asset management. For further information on our approach to transition risks please see our net-zero framework [here](#) and our principles below. Our framework has been developed in line with the Better Buildings Partnership (BBP) Climate Change Agreement.

The purpose of this document is to outline the work that the Long Lease Property Fund has undertaken to better understand the above climate risks, and set specific next steps within the context of the fund in addition to those outlined in the house strategy and investment process.

Figure 1: abrdn principles for net zero carbon delivery

Principles for Net Zero delivery			
Practical	Realistic	Collaborative	Measurable
<p>Regulatory compliance: align with energy performance compliance requirements which can be a sensible stepping stone in near-term</p> <p>Direct improvement: focus on improving quality of assets through energy efficiency and renewables – offsets only permitted for net zero claims to cover last 5-10% of abatement</p> <p>Timing: align improvements with existing plant replacement cycles and planned refurbishment activities wherever possible</p>	<p>Targets: long-term targets must be ambitious but deliverable and complimented by near-term targets and actions</p> <p>Policy support: to fully decarbonise before 2050 the real estate sector requires a supportive policy mix to incentivise action and level the playing field</p>	<p>Occupiers: net zero can't be achieved in isolation. Work closely with occupiers, many of whom have their own decarbonisation plans</p> <p>Suppliers: clear roles and responsibilities for all parties involved in managing assets – consultants, property managers, agents etc.</p>	<p>Monitoring/ review: clear key performance indicators and monitoring procedures at the asset and portfolio level</p>



About the Long Lease Property Fund

As abrdn's largest real estate fund, and an in-house ESG pioneer fund, we continue to focus on developing our strategy to move the fund to a net-zero carbon position. The fund's assets are typically single-let assets on a full-repairing and insuring (FRI) lease. Our ability as landlords to influence energy consumption – or even capture energy, water and waste data – has been challenging in the past. However, we don't believe this should prevent us from striving to reduce the fund's carbon impact.

We've already seen a huge mindset change regarding net-zero transition from the vast majority of our tenants. They're increasingly willing to work with us, in terms of the data we collect and exploring using renewable energy initiatives. As a result, we've moved our level of energy data collection from around 35% of the fund (measured as a percentage of the fund's total floor area) for our 2018 submission to the Global Real Estate Sustainability Benchmark (GRESB) submission to 93% for our 2022 submission. We are also laying the foundations

to improve on this again during next year's GRESB reporting submission, by targeting those tenants that have been the least engaged to-date on ESG issues. This increase in data capture reflects both the increased engagement and changing attitudes from our tenants towards all ESG-related matters. In addition, we have a variety of Solar-PV (photovoltaic) systems at various stages of implementation and a range of other ongoing conversations regarding ESG measures with a number of tenants.

ESG considerations are now firmly embedded at the heart of our investment process which can be seen through our investment activity in 2021 when every asset we acquired was either an EPC (Energy Performance Certificate) A or B, or had an action plan to reach a rating at this level. On the disposals side, we have been actively selling assets which have poorer ratings and where we have concerns over their longer term ESG position.



Transition risks: Our net-zero carbon strategy

Setting the ambition

The fund has undertaken detailed carbon modelling with the support of the external consultant Verco. This has involved a full review of the fund, asset by asset, understanding carbon performance, identifying where improvements could be made and how much they will cost. It has enabled us to benchmark energy consumption and carbon emissions for each asset and allow us to carry out sensitivity analysis in achieving reductions for both 1.5° and 2° temperature change scenarios alongside a Business As Usual (BAU) scenario. This piece of work has helped us to determine the net-zero carbon strategy of the fund and next steps to work towards this.

Following the carbon modelling insights, the fund is targeting net-zero carbon by 2050 for scope 1, 2 and 3 emissions. The Fund will also consider balancing its residual carbon emissions from 2040 onwards with high quality nature-based carbon removal and reduction units; and co-deliver additional biodiversity and social impact.

As part of this target and strategy:

- The fund will initially use the CRREM (Carbon Risk Real Estate Monitor) 1.5 pathway to track progress, however this will be reviewed as further science-based pathways are developed or updated.
- The fund will follow a location-based approach for calculating carbon emissions. This will be reviewed according to the evolution of best practice in the market.
- The fund will report its carbon emissions annually and report progress.
- As the fund mandates specific target returns, the fund recognises that there is currently a gap between the policy and the science to achieve net-zero and that this net-zero target will be focused on as much as the market will allow with regards to the investment performance target.
- The Fund recognises that it is unlikely that net-zero will be reached by reduction alone. As a result, the Fund will consider offsetting its residual carbon from 2040 onwards with high quality nature-based carbon credits.
- The fund will follow industry standard definitions of net-zero which currently dictate that net-zero cannot be claimed unless a 90% reduction has been achieved with the option to offset the remaining 10%, but this may evolve over time.



¹ Residual carbon is the carbon emissions above those specified in the reduction targets of achieving a net-zero pathway.

The baseline

The portfolio comprises single-let FRIs, which are tenant-controlled (indirectly managed). Therefore, all operational energy is procured by the tenant; and the associated carbon emissions fall under "Scope 3" in line with the GHG (greenhouse gas) Protocol. The only exception to this is where the unit is vacant, in which case the fund directly procures the energy for the period of vacancy which is typically very low. The carbon accounting approach undertaken for the fund is aligned with the operational and whole building approach.

for 77% of the portfolio by floor area, with representative industry standard benchmarks used to estimate the rest. Based on these assumptions for 2019, the energy intensity at the portfolio level was 210 kWh/m² and the operational emissions intensity was 47 kgCO₂e/m². These will be key metrics as we progress with our delivery strategy.

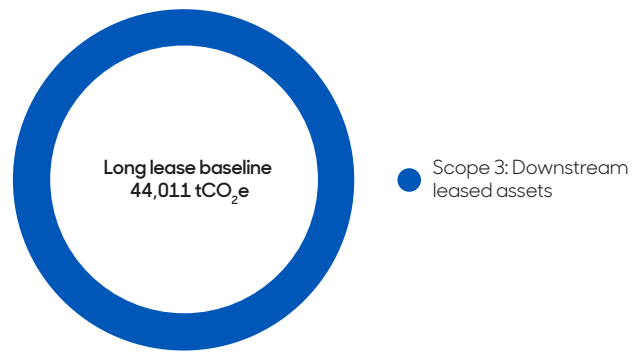
Figure 2: Long Lease Property Fund baseline carbon footprint for the reporting year of 2019; comprising entirely Scope 3 GHG emissions from downstream leased assets

Carbon baseline

We have used 2019 as a baseline as it was unaffected by changes in occupancy due to COVID-19.

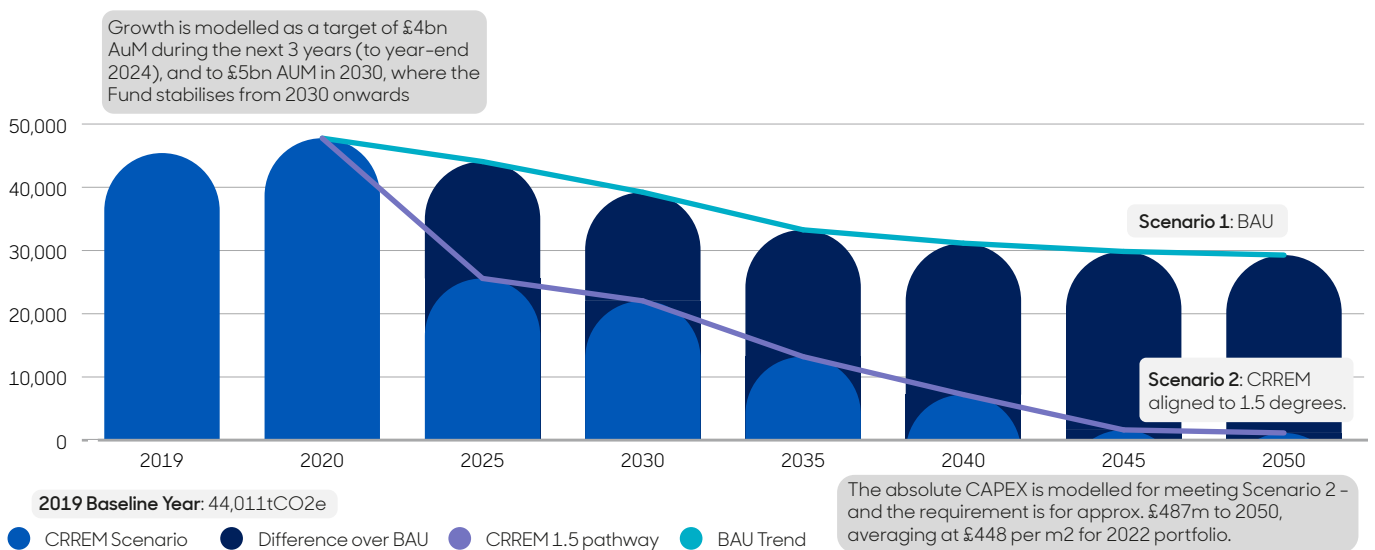
Our operational carbon footprint for 2019 is shown in Figure 2.

This shows a total operational footprint of 44,011 tonnes of carbon dioxide equivalent (CO₂e). Of this, 100% is Scope 3 emissions from tenant-procured energy (there were no recorded Scope 1 and 2 emissions from the Fund in 2019). For 2019 we had actual energy consumption data



Source: abrdn.

Figure 3: Long Lease Property Fund carbon operational emissions forecast from 2019–2050 modelled under two scenarios (1) Business as Usual including UK forecasts of grid decarbonisation and (2) Meeting the CRREM 1.5-degree pathway



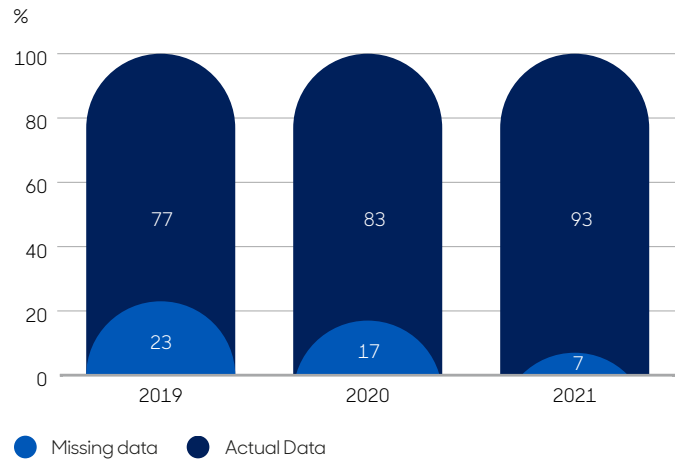
Source: abrdn.

Carbon reporting

In addition to the 2019 baseline work, we have also reported in this section carbon data for the 2019, 2020 and 2021 calendar years, which is aligned with our GRESB submissions for the same three periods. Primary (actual) data coverage (data obtained from the tenants) accounted for 93% of the total floor area for 2021, compared with 83% in 2020 and 77% in 2019. While estimation and reporting of missing data was completed in 2019 as part of Verco's net-zero analysis work, no estimates of missing data has been completed for 2020 and 2021 at this stage. However, Verco are currently working with us to estimate the missing data and validate the actual data, which will be reported to our stakeholders when available for 2021. Such estimations will be completed using industry-accepted UK energy-intensity benchmarks. We hope to improve the percentage of actual data in future reports, with the aim of achieving 100% coverage of 'actual' data from tenants.

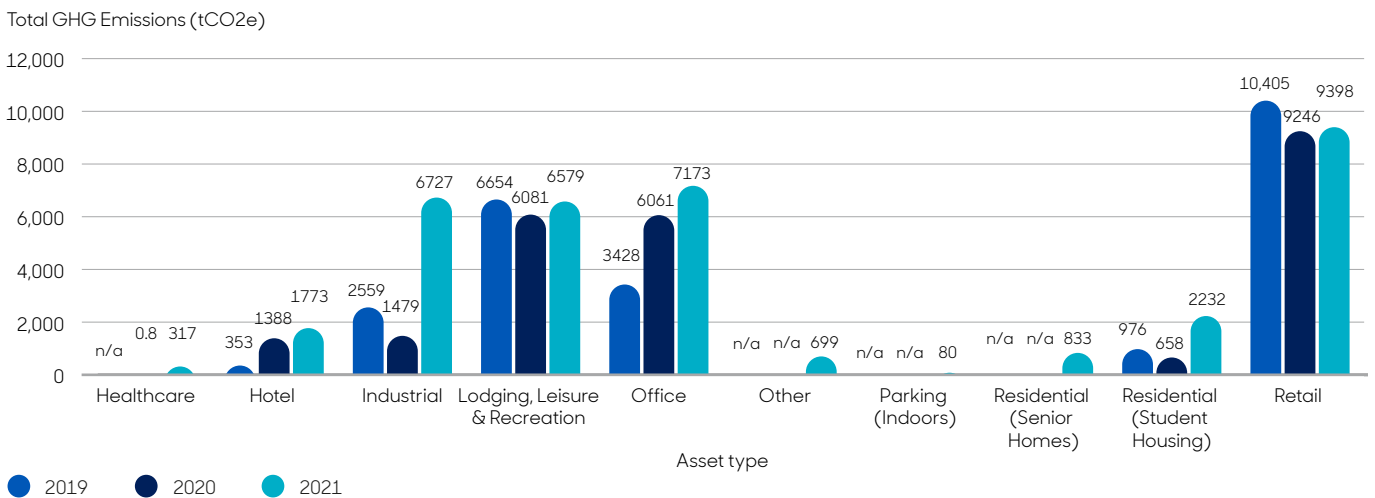
Data has been provided below for 2019, 2020 and 2021 on an 'absolute' basis and for 2020 and 2021 on a 'like for like' basis. On a like-for-like basis for 2020 and 2021, Scope 3 GHG emissions increased by 2.1% year-on-year. This increase was primarily driven by assets in the Industrial, Lodging, Leisure & Recreation and Student Housing sectors, and attributable to increased operation as a result of relaxation of Covid-19 related lockdown measures throughout 2021.

Figure 4: GHG emissions – Coverage of actual data (2019-2021)



Source: abrdn.

Figure 5: Absolute GHG emissions (Actual Data) 2019-2021



Source: abrdn, as at 2021.

Figure 6: Absolute GHG emissions by property type (Actual Data) 2019–2021

Asset Type		GHG emissions (tCO ₂ e)			GHG emissions intensity (kgCO ₂ e/m ²)		
		2019	2020	2021	2019	2020	2021
Healthcare	Scope 2 & 3	n/a	0.8	317	n/a	1.3	48
Hotel	Scope 2 & 3	353	1388	1773	32	29	26
Industrial	Scope 3	2559	1479	6727	42	11	32
Lodging, Leisure & Recreation	Scope 3	6654	6081	6579	4.0	3.2	3.5
Office	Scope 3	3428	6061	7173	80	70	66
Other	Scope 3	n/a	n/a	699	n/a	n/a	4.0
Parking (Indoors)	Scope 3	n/a	n/a	80	n/a	n/a	1.2
Residential (Senior Homes)	Scope 3	n/a	n/a	833	n/a	n/a	48
Residential (Student Housing)	Scope 3	976	658	2232	785	252	55
Retail	Scope 3	10405	9246	9398	108	96	95
Total	Scope 2 & 3	24375	24914	35809			

Source: abrdn, as at Dec 2021.

Data qualifying notes

GHG emissions were calculated in line with the Greenhouse Gas Protocol using the location-based emissions factors methodology.

Scope 3 allows for the treatment of other indirect emissions that are a consequence of the activities of the reporting company, but occur from sources owned or controlled by another company, such as tenants. (The Greenhouse Gas Protocol Initiative, World Resources Institute). Note that any Scope 2 emissions referenced in this table relate to emissions from void (vacant) units only, where the responsibility for any energy consumption falls to the landlord (c.f. tenant). No scope 1 emissions are reported as they did not apply during the reporting periods. Where emissions are quoted as "n/a", either no data was collected for this asset type in the reporting year, or the asset type was not present in the Fund in the reporting year.

Figure 7: Like for like emissions by property type (Actual Data) 2020 and 2021

Asset Type		GHG emissions (tCO ₂ e)		GHG emissions intensity (kgCO ₂ e/sq.m)		
		2020	2021	% change	2020	2021
Hotel	Scope 2 & 3	1388	1285	-7	29	27
Industrial	Scope 3	1479	1641	11	11	12
Lodging, Leisure & Recreation	Scope 3	6081	6579	8	3	3
Office	Scope 3	6061	5756	-5	66	62
Residential (Student Housing)	Scope 3	619	1276	106	453	933
Retail	Scope 3	9246	8858	-4	96	92
Total	Scope 2 & 3	24874	25395	2.1		

Data qualifying notes:

GHG emissions were calculated in line with the Greenhouse Gas Protocol using the location-based emissions factors methodology.

Scope 3 allows for the treatment of other indirect emissions that are a consequence of the activities of the reporting company, but occur from sources owned or controlled by another company, such as tenants. (The Greenhouse Gas Protocol Initiative, World Resources Institute). Note that any Scope 2 emissions referenced in this table relate to emissions from void (vacant) units only, where the responsibility for any energy consumption falls to the landlord (c.f. tenant). No scope 1 emissions are reported as they did not apply during the reporting periods. Where emissions are quoted as "n/a", either no data was collected for this asset type in the reporting year, or the asset type was not present in the Fund in the reporting year.

Meeting our net-zero commitments



We are confident that abrdn’s multi-faceted approach to ESG will allow us to deliver on our net-zero commitment. As one of our pioneer funds within real estate, the Long Lease Property Fund will be at the forefront of progressing this strategy. We hope the data provided in this report will give our investors confidence that the fund is well on the way to achieving this aim. Key actions for the fund are summarised below and in the following table.

Improving carbon reporting: Carbon reporting is constantly evolving. We currently produce a standalone report, but in time our aim is to consolidate this into our client reporting process. We are working hard to integrate mechanisms to maximize our data coverage; including green leases and smart metering; all with the aim of maximizing data coverage, which will allow us to model our net-zero pathway with a greater degree of accuracy.

Stakeholder Engagement: Working closely with our tenants to bring them on the journey with us is a hugely important part of this process. Our engagement with tenants on the importance of ESG factors is now paying dividends. As mentioned, there has been a marked increase in the data we’ve collected from them between 2018 and 2022. In addition, we’re also seeing a growing number of tenants actively discussing with us ways they can improve the green credentials of the buildings they occupy. However, we can always work to improve on the success to date and continue to work with our tenants in exploring various opportunities to improve the ESG credentials of our assets, primarily, but not exclusively, considering opportunities at reducing energy demand.

To make the fund a net-zero entity, we know we must make changes. That means investing a considerable amount of time and effort on all aspects of ESG. We also can’t do this without the cooperation of our tenants – so it’s crucial we work closely alongside them. The payback period or economic life of some of the technologies we are exploring at an asset level are around 15–20 years; which complements the long-leases that the vast majority of the Fund’s occupiers are on. This means there are benefits on all sides and we can work in tandem with our tenants to reduce the carbon emissions of the assets we hold. In terms of any new investments by the fund, we now expect assets to have very high ESG credentials before we will consider any acquisition. In fact, we are now dismissing investment opportunities solely on ESG grounds especially where we understand the ESG risk to hinder investment performance now and in the future.

Overall, the fund is in a good position to move forwards given our level of existing data capture, and we are hopeful the nature of the longer leases we invest in will provide us with an opportunity to work with our tenants to ensure we are striving to reduce our environmental impact.

Figure 8: Net-zero actions and performance to date for the Long Lease Property Fund

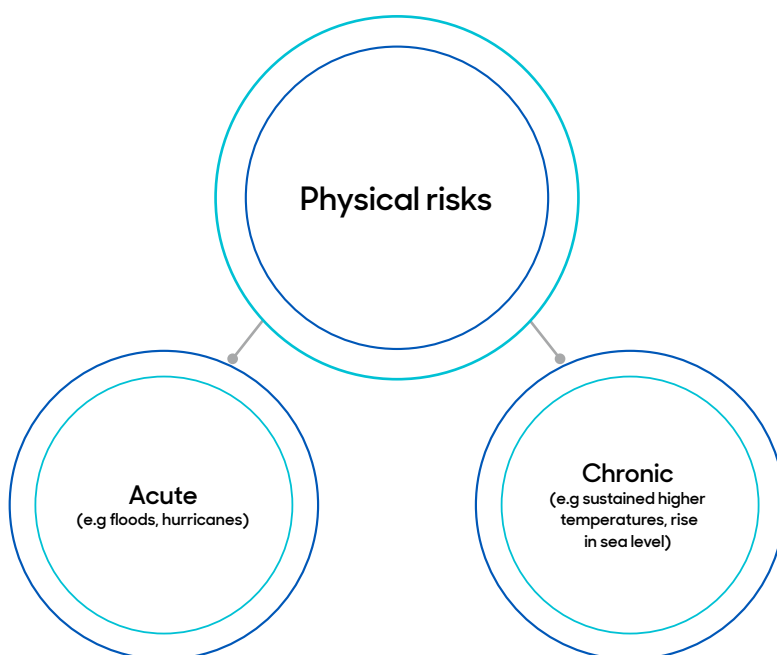
	Action	Performance to date (at Q4 2021)
Standing portfolio	<ul style="list-style-type: none"> Improve coverage of tenant energy data through improved engagement, lease agreements and smart metering. 	<ul style="list-style-type: none"> 93% data coverage by floor area. 100% of tenants engaged through written communication.
	<ul style="list-style-type: none"> Build improved understanding of tenant decarbonisation strategies and extent of renewable energy procurement. 	<ul style="list-style-type: none"> 22% of tenants additionally engaged with in-person meetings specifically on ESG.
	<ul style="list-style-type: none"> Implement low-carbon refurbishment to ensure regulatory compliance focusing on energy efficiency and heat decarbonisation and start to quantify embodied carbon. 	<ul style="list-style-type: none"> 4% of assets (by number) have no gas. 43% of estimated rental value (ERV) with EPC A-B ratings.
	<ul style="list-style-type: none"> Implementation of Solar PV projects. 	<ul style="list-style-type: none"> 10% of assets (by number of assets) with Solar PV. 2,442,401 kWh of renewable energy generated in 2021.
Acquisitions and developments	<ul style="list-style-type: none"> Benchmark assets pre-acquisition, understand costs and build decarbonisation into asset management plan from the start of ownership. Direct developments and development fundings to be designed to whole-life net-zero principles where feasible. 	

We’re not done yet: We are proud of the progress made by the fund to date, and the results are a testament to the excellent team we have and the relationships we have with our tenants, but we don’t intend to rest on our laurels. We will continue to work with our tenants to increase the level of data we receive across the portfolio, in addition to exploring further green initiatives.

Physical risks

Whilst mitigating climate change as much as we can through our net-zero approach, and being as prepared as possible for transition risks, we also need to be prepared for the future physical risks of climate change which might impact our portfolio.

Figure 9: Types of physical climate risk



We have already undertaken initial work to start understanding the impacts of physical risks and will expand on this in the future:

Figure 10: Delivery framework for addressing physical climate risks

	Work to date	Future work
Standing investments	Modelled the implications of a worst-case scenario Representative Concentration Pathway (RCP) 8.5 (+4 degrees) looking at both chronic (3 hazards) and acute (4 hazards)	To re-model the assets under three or more scenarios aligned with abrdn bespoke scenarios
Acquisitions	Currently assess flood risk	We have recently updated our acquisition approach to include comprehensive screening across 8 physical climate hazards, which can be assessed across multiple time horizons (current, 2030, 2050 and 2100) under three climate change scenarios (ranging from Representative Concentration Pathway (RCP) 2.6 to 8.5).

Summary

The Long Lease Property Fund is committed to working towards net-zero, and its managers understand the importance of ESG to all of its stakeholders. We have put together a realistic plan in order to achieve our ultimate goal of being net-zero by 2050 and look forward to continuing to capitalise on the excellent tenant relationships that we have in order to achieve better outcomes. Accordingly, this means working with them to improve all aspects of ESG in relation to every asset in the fund and not just focussing on headline environmental matters like carbon reduction.



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Important Information

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The value of investments, and the income from them, can go down as well as up and clients may get back less than the amount invested.

Real estate is a relatively illiquid asset class, the valuation of which is a matter of opinion. There is no recognised market for property and there can be delays in realising the value of assets.

The sterling value of overseas assets held in the fund may rise and fall as a result of exchange rate fluctuations.

The views expressed in this document should not be construed as advice or an investment recommendation on how to construct a portfolio or whether to buy, retain or sell a particular investment. The information contained is for exclusive use by professional customers/eligible counterparties (ECPs) and not the general public.

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