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MIS"LEED"ING: FACT VERSUS FICTION FOR GREEN BUILDINGS



How many times have we heard those worn-out taglines of 'sustainability,' 'green is good,' 'triple bottom line,' and 'doing well by doing good?' Study after study, report after report, and headline after headline. All used to help justify products like electric vehicles and solar panels, as well as to defend related policy mandates, market protection, and subsidies.

Many of today's largest markets and industries rely entirely on the ability of the expert class to continue to hoodwink consumers, taxpayers, and investors on the false need and an altered reality of certain products and standards.

Consider the case of green building design, specifically LEED-certified buildings.

For those unfamiliar with LEED, it stands for 'leadership in energy and environmental design.' It's become all the rage in real estate these days, particularly for commercial and office space. LEED-certified buildings enjoy an unchallenged reputation for better performance, accretive economics, and societal benefit.

That's due in large part to an ocean of studies that posit LEED-certified buildings as superior to non-LEED-certified buildings in every imaginable way.

CREATING THE NEED FOR LEED

A recent example is the October 2022 research report from real estate firm CBRE titled ***Green Is Good: The Enduring Rent Premium of LEED-Certified U.S. Office Buildings***.

The title is an eco-marketing thing of beauty; a rich, concentrated trove of all the gimmicky tricks. Employ an obligatory worn-out tagline ('green is good')? Check. Inject an aura of economic legitimacy ('rent premium')? Check. Infer a longevity that exceeds the half-life of CO2 in the atmosphere ('enduring')? Check.

The executive summary doesn't disappoint. It begins by boldly stating that an analysis of 20,000 office buildings in America found that the average rent of those with LEED certification was 31% higher than those of non-LEED-certified buildings.

The impressive finding indicates that renovating existing or building new spaces that have high energy efficiencies and meet LEED certification standards are well worth the effort and investment.

Except, when digging a little deeper into the study's details and data, that's not exactly the case. In fact, that's not at all the case.

THE DEVIL IN THE DATA

As with many studies, reports, and news articles surrounding the vaunted energy transition, reading beyond the title and executive summary is vital. Doing so for this study of the economics of LEED-certified buildings betrays a very different set of conclusions than the popular consensus and the report's title.

The golden rules of real estate, including the ultimate of location-location-location being the three most important factors determining value, apparently still matter today, even with Code Red for humanity and approaching climate doom.

When the study's data are adjusted under regression analysis for building location, building age, and renovation history, the premium that LEED-certified buildings enjoy shrinks from the advertised 31% down to just under 4% before COVID and only 3% after COVID.

That's a massive drop to a paltry, low single-digit premium that may be within the statistical noise and uncertainty of the study. Meaning when an apples-to-apples comparison is performed, LEED certification doesn't amount to much of any appreciable rent premium.

Building age is far more impactful than LEED certification. The regression analysis found that office assets built after 2012 commanded a 14% rent premium over those that were built between 2002 and 2011. Each additional decade in age decreased rent by approximately 5%.

Data prove age affects rent much more than LEED certification.

What's intriguing is that the complete report disclosed these findings and how they evaporated the trumpeted rent premium for LEED certification. It's all in the body of the report, which very few people take the time to read.

By the way, LEED-certified office buildings tend to be larger and higher quality assets concentrated in downtowns of expensive cities, compared to non-LEED-certified buildings. Which means LEED-certified spaces should enjoy higher rent premiums than buildings that are smaller, lower quality, and not located in the most exclusive of zip codes.

The report cites that a third of Manhattan's office inventory is LEED-certified while only a tenth of Louisville's office inventory is LEED-certified. And Manhattan office space is pricier than Louisville's. Yet rent premiums of Manhattan offices versus Louisville offices have very little to do with whether the buildings are LEED-certified. It's because it's Manhattan and Louisville!

VOODOO ECONOMICS

What you don't find discussed in the study, which harms its credibility, is recognition that constructing a LEED-certified building is a more expensive proposition in up-front capital investment than constructing or renovating a non-LEED certified building. If there is only a miniscule, or nonexistent, rent premium for the LEED-certified office, the rate of return will indicate a losing investment proposition, not a winning one. That is the opposite conclusion that the study's title warrants.

The study also argues green buildings offer lower mortgage default risk for investors. That may not be the case looking forward into the coming years, when considering LEED-certified buildings are disproportionately concentrated in at-risk real estate bubble markets of Manhattan, San Francisco, and so on.

Further, LEED certified buildings are a favorite of the tech industry. And the tech industry right now is on the verge of a major correction, with job losses piling up and with office buildings, many LEED-certified, being vacant and leases being abandoned. LEED-certified buildings may post higher default rates than traditional offices as we experience the grips of a recession or slowdown, or certainly if another tech bubble bursts.

Unaddressed in the study and regression analysis is what impact government leasing of LEED-certified buildings has on rent spreads. One of the largest tenants of metropolitan office space is often government. If bureaucrats favor LEED-certified space and aren't afraid to pay up with taxpayer dollars to rent it, rent spreads for LEED-certified buildings are likely to skew. Without government subsidy, there may be no rent premium for LEED certification. Perhaps, there might even be a 'green discount'.

COMMUNAL PARADISE LOST?

There are other flaws in the study.

It wrongly assumes de facto 'increased productivity' associated with LEED-certified buildings. That's not obvious or necessarily true for the workers who inhabit them. Ledger entries of debits and credits by accountants working in a LEED-certified building don't

magically happen quicker or more accurately than they would when the accountant is working in a non-LEED-certified building.

There's another false premise about LEED-certified buildings, particularly in the era of pandemic: the health and wellness benefits associated with LEED-certified buildings. Today, there are health risks found in LEED design features.

For example, are low-flow water faucets in restrooms of LEED-certified buildings a health risk when it comes to hygiene and germ spread? A similar question pertains to HVAC systems in LEED-certified buildings that try to balance energy efficiency targets with fresh air-to-recirculation air ratios.

These days, most office occupants do not relish the thought of breathing air all day that has longer average indoor residence time. Or using faucets that trickle to wash hands. The safer office building environment would employ higher water flows in restroom faucets to minimize germ transfer and HVAC systems using as much fresh air feed as practical.

And those celebrated common areas for collaboration, meeting, and eating utilized in LEED-certified buildings? Just another venue for potential disease transmission.

Pandemic necessitated a re-think of all facets of life and business. Yet LEED-certified design has largely escaped such a re-think. Why? Aspects common in, or mandated by, LEED certification need an objective reassessment as to whether they are beneficial in the era of Covid.

TOO MUCH OF A GREEN THING

A key conclusion buried in the study escaped mention in the executive summary and title. The regression analysis found no statistically significant rent premium associated with higher levels of LEED certification.

Attaining a higher level of LEED certification requires more investment to achieve the target level of points. If there is not a statistically significant rent premium associated with higher LEED certification, then being greener is not better. Being greener is a poor investment decision; investors lose money when spending to attain a higher level of LEED certification.

THE ECHO CHAMBER AT WORK

How one stumbles upon this report is emblematic of how the echo chamber works in media, the expert class, and environmentalism today.

A headline on a major business website mentioned the study title, specifically the 'green is good' hook. The website article exclusively highlighted the report's title and the opening statement of the executive summary that advertised the massive 31% rent premium for

LEED-certified buildings. Only until tracking down the study and reading the body of the report will the regression analysis come to light.

That’s how the environmental racket operates these days. The green formula:

- Perform a study to skew in the desired direction by applying favorable assumptions.
- Push the desired findings in the executive summary.
- Come up with a creative and eye-catching title (use those eco-taglines we called out in the beginning), then post or publish the report.
- Collaborate with major media to rebroadcast and further amplify the desired sound bite or headline.

It’s not greenwashing. It’s worse. Most would consider it misleading and unethical.