

Responsibility in practice



Integrating responsible property investment

July 2015

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Report coverage, material aspects and boundaries

The purpose of this report; The Hermes Real Estate's 2015 Responsible Property Investment report, is to describe our approach to RPI governance, strategy and management within our portfolio with a focus on the areas of our operations that have been identified as material. We report our responsible investment governance, strategy and management approach for our whole portfolio through a narrative approach. This includes our directly managed and indirect assets that we have influence over in the UK and internationally for the period June 2014 to June 2015. We engage and monitor our indirectly held portfolios through active engagement and by using the GRESB survey responses. We report key environmental and social performance indicators for our UK assets over which we have management control for the period January 2006 to December 2014.

For more details visit: www.hermes-investment.com/realestate/overview

Reporting standards

This report contains Standard Disclosures from the Global Reporting Initiative (GRI) G4 Core Guidelines. In particular the following sections are developed in accordance with G4 Core requirements:

- Assessment of material aspects: relate to Report coverage and the RPI integration graph (p.4-5).
- "Economics indicators" relate to Who we are (p.1) and Financial Savings (p.23) sections
- "Environmental Indicators" are found in Active Management (P.16-18) and Environmental Performance sections (p.23-25)
- "Social indicators" are found under:
 - "Labour Practices and Decent Work" relate to both Code of Ethics (p.7) and Supply Chain (p.8) sections
 - "Ethics and Integrity", "Human Rights" relate to the Code of Ethics section (p.7)
 - "Society" can be found in the Community (p.20-21), Working with Occupiers (p.17), and Sector Engagement (p.9) sections
 - "Product Responsibility" is in our Active Management section (P.16-18)

Advisor's Statement

In 2014 Carbon Credentials supported Hermes Real Estate in the delivery of their Responsible Property Investment programme. This included the collation, validation and reporting of sustainability performance data and property characteristics. The greenhouse gas emissions and energy data in this report has passed ISO 14064-3 greenhouse gas verification, as performed by the independent assurance team within Carbon Credentials. As such, we understand the information in this report to accurately reflect the current performance of the RPI programme.

Our aim has been to support the ambition and drive of the RPI programme. Vital to the programme succeeding through the whole value chain is ensuring that policy and strategy is clearly articulated to the property managers and that it aligns to operational process. Likewise, visibility of performance must move upward through management. Fund and asset managers must have access to performance information which is clear and easy to interpret, so that they can make informed decisions. Hermes Real Estate's RPM programme has this information cycle in place, and as we move forward we will continue to refine and improve it – adding more context to provide greater value insight.

This year there has been a large influx of new assets into the Hermes Real Estate portfolio. This has subsequently impacted the absolute emissions, which have increased by 62%. However, the track record of the effect of the RPI programme clearly shows that these acquisitions are an opportunity to improve the management and performance of these buildings.

Sam Carson, Director of Sustainability Innovation, Carbon Credentials

Who we are

Institutional investment manager working to deliver excellent, long-term, performance – responsibly

At Hermes Real Estate, part of Hermes Investment Management¹, we are an active asset manager working to deliver excellent, long-term, performance – responsibly. We aim to lead the debate and contribute to the transformation of the investment industry, to the benefit of our clients, their stakeholders and, ultimately, society at large.

Hermes Real Estate in numbers

**1985
-2015**

Established

Investing in Real Estate for the last
30 years



Assets under management

£7.0bn Gross Asset Value (GAV)²



Offering

Client-focused, property investment
solutions



Geographical coverage

UK, Europe, Americas, Asia Pacific



Segregated and unitised solutions

BT Pension Scheme (BTPS) direct property portfolio,
Hermes Property Unit Trust (HPUT), HUH US
Real Estate income fund, Hermes Central London
Limited Partnership (HCL LP), Metro Property Unit
Trust (Metro), Argent market leading UK developer,
MEPC specialist investor in business estates,
The centre:mk LP, NOMA LP.



Team

22 property professionals with
20 years' average industry
experience

Awards

Hermes Real Estate is a recognised industry leader with both an innovative and long term approach to responsible property investment.



As at end-March 2015, the Hermes Property Unit Trust delivered a top quartile return to investors over 1, 3, 5 and 10-year periods and was the top performing fund within its benchmark over 5 and 10 years. The Trust also won a performance award at the IPD/IPF Property Investment Awards 2015 for the highest 3-year return to December 2014 on a risk adjusted basis within the Balanced Funds category.



Hermes Real Estate has been awarded the UK Property Manager of the Year – Professional Pension Investments Awards 2014.



A leader in responsible investment Hermes Real Estate has been awarded 4 GRESB Green Stars in 2014.

¹ On behalf of our clients, we manage £30.1 billion as at 31 March 2015 and we advise on over £124.3 billion through our ESG and stewardship services. Note the total AuM figure includes £3.5bn of assets managed or under an advisory agreement by Hermes GPE LLP ("HGPE"), a joint venture between Hermes Fund Managers Limited ("HFM") and GPE Partner Limited. HGPE is an independent entity and not part of the Hermes group. £0.5bn of total group AuM figure represents HFM mandates under advice.

² Hermes Real Estate as at 31 March 2015, £6.4bn NAV.

Note: Performance over 1 year is annualised.

Responsibility: A core value



■ By integrating responsibility in our investment process we act in the long term interest of our clients while striving to improve the economy, communities and the environment they invest in. ■

Chris Taylor

Chief Executive Officer, Hermes Real Estate

Hermes Investment Management

Our culture

Since inception in 1983, Hermes has been owned by and acted as the principal investment manager for the BT Pension Scheme – the UK's largest corporate pension fund.

Our ownership by the scheme and our duty to serve its 320,000 pensioners gives us a strong sense of fiduciary responsibility which is embedded throughout the firm and which informs the decisions we make and the actions we take. It also gives us an unrivalled insight into the long-term needs of savers and helps us develop investment strategies that will enable them to meet their goals.

Our responsibilities

Behaving responsibly is important to us and not limited to the way we manage money for our clients. We have a strong focus on environmental, social and governance issues and participate fully in industry and sector initiatives to develop best practice. We believe that influencing companies and public policy in this way produces better long-term returns for shareholders and investors. Our specialist engagement team, Hermes EOS, advises on over £124bn of investments, making Hermes one of the leaders in this field.

Beyond this, we believe in acting responsibly as a company in all aspects of our business. We have a strong corporate social responsibility programme that is focused on helping the communities in which we live and work. We have ISO14001 accreditation and we adhere to the London living wage. We also provide pro-bono support for the independent 300 Club, which was co-founded by our Chief Executive Saker Nusseibeh to challenge investment orthodoxy and improve the contribution of financial services to society.

Integrating responsible property investment in practice

The value in adopting responsible investment practices, such as consideration of the sustainability characteristics of buildings, for example, has become an established market trend in real estate investment. This trend is driven by studies across jurisdictions pointing to growing climate and sustainability regulatory pressure, an increasing understanding of the long-term physical, regulatory and market risks by institutional investors and rising occupier demand for green buildings. It is now widely recognised that responsible investment practices are changing real estate market conditions.

We have identified and reported on these trends for a number of years and have responded by progressively integrating Responsible Property Investment throughout our investment and asset management processes. We also continue to work with the industry to develop tools and methods to that effect.

In this report we illustrate how we have integrated our responsible approach in practice. We have achieved Responsible Property Investment (RPI) integration across our processes by developing dedicated tools and linking our corporate strategy and strategic investment targets with our portfolio strategies and the management of our buildings. This has been a continuous and evolving process aligned with best practice as proposed by leading institutional investors³. We also have an active programme of internal and sector wide initiatives to develop the tools, benchmarks and knowledge required for an effective integration and comparison of performance at fund and market level.

The graphic overleaf provides a schematic view of our approach and processes. In the following sections of this report we will illustrate through initiatives, case studies and performance data the different steps of this approach across our organisational levels and the results that this has enabled us to deliver.



Image: Elliot House, Manchester. The off-market acquisition of a freehold office and restaurant building situated directly opposite the Spinningfields business district. The office space has undergone a full refurbishment and the ground floor restaurant is pre-let and is undergoing a full refurbishment.

³ UNEPFI, IIGCC, RICS, PRI, May 2014: "Sustainability metrics: Translation and impacts on property investment and asset management", http://www.unepfi.org/fileadmin/documents/UNEPFI_SustainabilityMetrics_Web.pdf

Responsible property investment in practice

Sustainability and responsible investment tools are integrated throughout our investment and asset management processes and sustainability data is shared and connected between the various organisational levels of our investment and asset management processes.



This is important because: There are major benefits in implementing a comprehensive RPI programme across organisational levels and connecting principles and practice. They range from an improved ability to manage risks and capture opportunities, to increasing transparency and responding to client demands.



Responsible supply chain

Working with and rewarding contractors to maximise impact of responsibility programme across areas where they have control and influence.



Sector and public policy engagement

Sharing best practice and influencing the market to promote acceptance and implementation of responsible investment principles.

Portfolio Level

Investing responsibly



Valuing sustainability

Working with valuation professionals and adopting our internal investment models to integrate RPI considerations in the assessment of value.



Sustainability benchmarks

Developing dedicated sustainability benchmarking and reporting tools to improve management and the monitoring of funds' sustainability performance.

This is important because: Integrating responsibility principles into discounted cash flow models and the valuation portfolios strengthens risk management frameworks whilst redirecting capital towards opportunities to develop commercially sound and sustainable assets.



Working with occupiers

Advocating green leases and tenant engagement programmes to enhance environmental and social performance.



Investing in communities

Investing in community programmes to deliver mutual social and community benefits.

Performance data to support decision making.

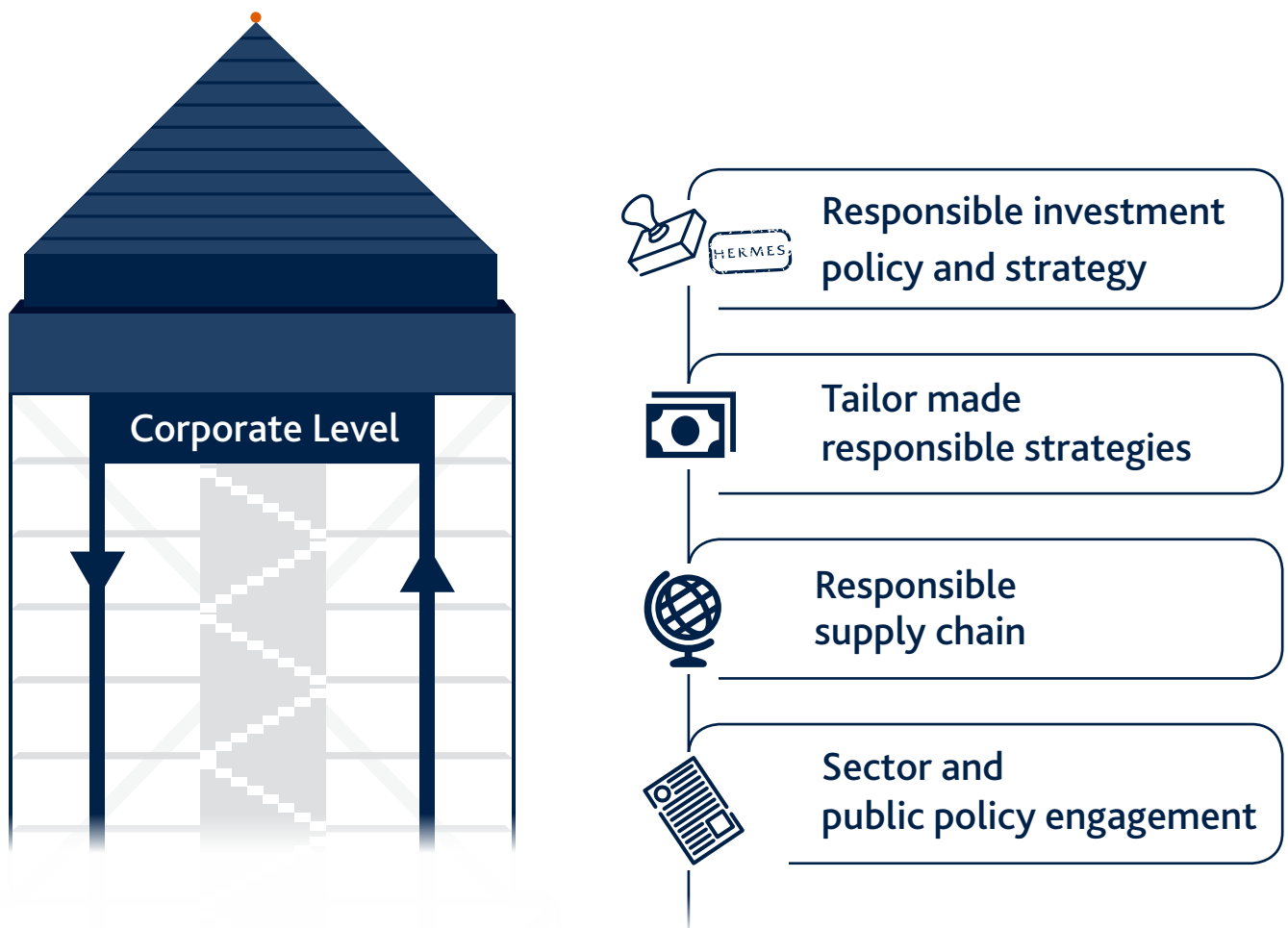
Corporate level

Driving responsibility

Comprehensive RPI programme: Major benefits across organisational levels

We have found there are major benefits from implementing a comprehensive RPI programme across organisational levels whilst also linking it to the appropriate aspects of various investments processes. These aspects span from governance, strategy and targets, stakeholder and sector engagement down to risk assessment, monitoring, comparability and reporting across portfolio and throughout the industry. These benefits include:

- Improved ability to manage risks and to capture opportunities to improve long term performance.
- Improved transparency and comparability across the market, enabling asset owners to better engage with investment managers on the implementation of responsible investment.
- Growing interest from clients, with RPI integration being assessed early during the investment manager selection process.





Responsible investment policy and strategy

Our investment style and philosophy

We are committed to acting consistently and clearly as stewards of the assets in which we invest, with the aim of delivering investment excellence. With a strong focus on income delivering returns and a disciplined approach to risk, we seek to consistently out-perform on a risk adjusted basis to deliver robust performance in line with our fiduciary responsibility to our clients. We see RPI risks as business critical to our clients and are committed to embedding responsible investment principles across our investment practices.

Our approach and governance structure is clearly defined in our policy and strategy documents and is integrated in our investment procedures. Our strategy aims to deliver buildings that anticipate and respond to market demands by understanding the needs of occupiers and communities as well as their assessments of real estate. This is strengthened by our understanding of the drivers of future performance in line with evolving regulatory frameworks. We comply with all current legislation and demonstrate preparedness for forthcoming regulatory requirements. We believe that responsible, long-term investment enables investors to manage RPI risks while capturing the social as well as the purely economic benefits of real estate.

Policy and strategy

Our RPI policy and strategy set a clear vision and objectives for our real estate clients with an emphasis on taking advantage of the opportunities offered by building responsibly. It includes targets, tools and minimum responsible investment requirements which are then clearly assigned to our investment and asset management teams.

Governance structure

A key part of our governance structure is our set of Hermes' policies approved by the Risk and Compliance Committee. These set out the minimum expectations that the company has towards its employees, partners or contractors. For example, we manage the risk exposures arising from bribery & corruption through dedicated policies and tools including risk assessments, employee training programme and due diligence at employee and procurement level.



Image: Leon Kamhi, Head of Responsibility, Hermes Investment Management

In charge of integrating responsibility principles across the business and educating all employees to the benefits of implementing Hermes ESG expectations.

Corporate level

Driving responsibility



Tailor made responsible strategies

Understanding and managing clients' expectations

Over the last few years there has been a new trend in asset owner's investment manager selection processes. A systematic review of RPI approach and programmes is now included as part of their due diligence process. We have found that Hermes Real Estate responsible investment expertise has featured prominently in a number of new clients' assessments of Hermes as an investment house.

On the establishment of real estate funds for new clients or of new joint-ventures, we develop tailor made responsible investment strategies and programmes that are then integrated into the new investment structures. This is done for our existing and new funds with targets and tools adapted to their market specificities. Our RPI approach is adapted to the constraints of our indirect investment with a focus on active engagement on governance, alignment of interests and fee structure, and sustainability performance.

NOMA's sympathetic and sustainable regeneration strategy

At the northern gateway to Manchester City Centre the NOMA development aims to sympathetically regenerate The Co-operative Group's historic home. The objective is to create a new smart, digital and sustainable neighbourhood and turn the currently neglected area into a destination location with a unique public realm and high amenity value to create a high quality, commercially led, mixed use destination.

In collaboration with our Joint Venture partner The Co-operative Group, a tailored NOMA sustainability strategy has been written embedding environment, social and governance aspects in all NOMA's real estate practices on a sound commercial basis.



Responsible supply chain

Working with and rewarding contractors

To enable maximum impact, RPI principles should be integrated throughout the supply chain and adopted in all areas where investment managers have control and influence. Through our code of ethics and corporate policies, we ensure that all employees have responsibility for ensuring Hermes complies and implements decent labour practices and work conditions and human rights principles. Our real estate supply chain policy ensures that our principles are included in our contracts with our property managers, refurbishment teams and surveyors and that in turn they require similar terms from their suppliers.

Hermes Real Estate RPI awards



Image: Award Winners 2014

Every year Hermes rewards its refurbishment teams, property managers, lawyers and consultants who have supported the delivery of its RPI programme by holding its annual RPI awards. The awards are the tip of the iceberg of our stakeholder engagement programme, demonstrating how we value working with all practitioners across the life cycle of the asset.



Sector engagement

Sharing best practice and influencing the market

We take an active role in public policy and sector engagement to promote acceptance and implementation of responsible investment principles across the real estate industry. This ensures sector-wide tools are developed enabling industry comparison and better monitoring of funds' performance.

We take an active and engaged role in the following organisations:

- Institutional Investors Group on Climate Change
- UNEP Finance Initiative
- British Property Federation
- Better Buildings Partnership
- Building Performance Institute Europe
- Global Real Estate Sustainability Benchmark

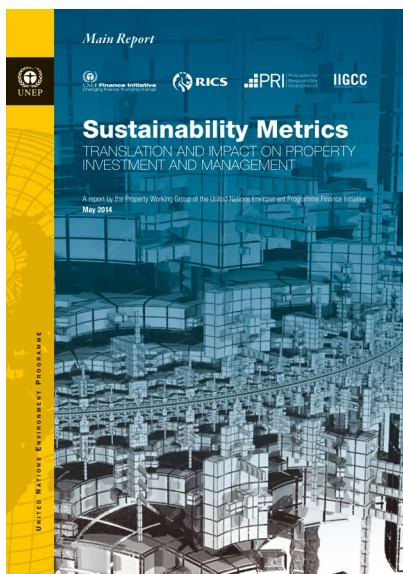


Image: UNEP FI Sustainability Metrics Report

Sector led tools and benchmarks

Over the years Hermes Real Estate has contributed actively to the development of the sector-wide sustainability tools and benchmarks listed below:

Better Buildings Partnerships (BBP) toolkits: Hands-on, practical toolkits to enable the uptake of sustainability in the built environment.

www.betterbuildingspartnership.co.uk

BBP Real Estate Environmental Benchmark: Based on the annual consumption data of BBP members property portfolios REEB provides energy, carbon, water and waste performance benchmarks for offices and shopping centres.

www.betterbuildingspartnership.co.uk

Energy Efficiency Finance Institution Group: Energy Efficiency the first fuel for the EU economy; market and policy recommendations to drive investments in energy efficiency in buildings and industry.

www.eefig.com

Global Real Estate Sustainability Benchmark (GRESB): Assess and enables peer comparison of the sustainability of whole real estate portfolios for property companies and real estate funds.

www.gresb.com

Global Reporting Initiative Construction and Real Estate Sector Supplement (GRI CRESS): Provides a global set of standardised indicators and reporting methodologies.

www.globalreporting.org

Institutional Investors Group on Climate Change, Trustees guide climate and sustainability reporting for property investment portfolios: Guide to manage environmental impacts of pension fund real estate portfolios.

www.iigcc.org

IPD Eco Portfolio Analysis Service: Sustainability investment risk of whole portfolio and comparison of exposure with other market players.

www.ipd.com

EPRA sustainability reporting guidelines: Simplified and standard methods for investment managers to report their sustainability performance.

www.epra.com

UNEP Financial Initiative et al 'Corporate sustainability management framework': An integrated sustainability metrics collection and management system.

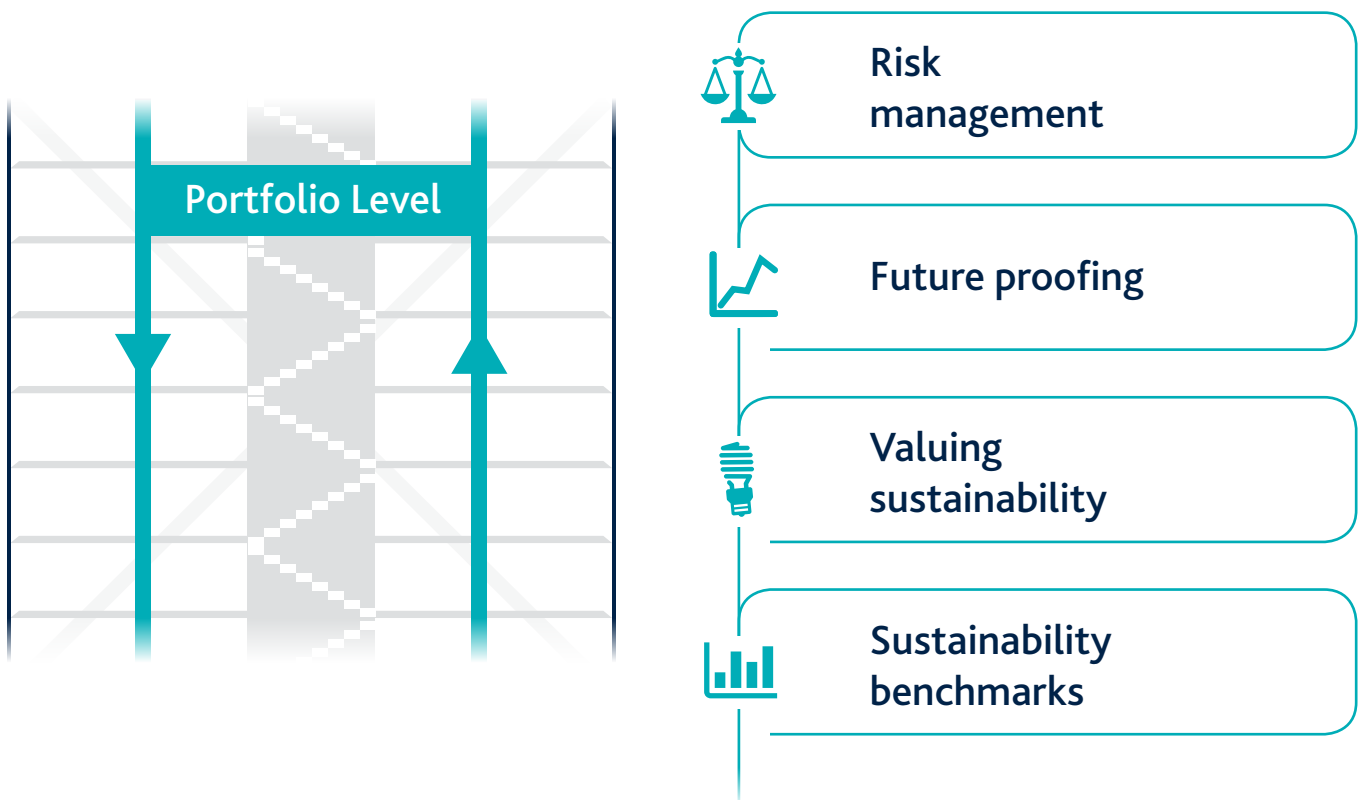
www.unepfi.org

Portfolio level Investing responsibly

In response to the changes in the market, the integration of RPI into real estate investments has made notable progress over the last few years. However, it is now time to integrate sustainability in portfolios investment management in earnest.

One of the key challenges is the need to be more explicit about how sustainability affects the value of individual assets and the risk of depreciation of entire portfolios. This means measuring how these factors impact on real estate investment performance and how they influence real estate market fundamentals, including client demand, void lengths, obsolescence, rate of depreciation, operational costs and liquidity. Tailored responsible investment strategies are required to match the characteristics of different portfolios and actively manage risks.

To do this, investors need to understand, measure and benchmark sustainability risks in earnest. This information then needs to be integrated into the discounted cash flow models of real estate investments and the valuation assessment of portfolios. This will allow current risk management frameworks to be strengthened whilst simultaneously unlocking and redirecting the capital required for the creation of commercially sound and sustainable assets.





Risk management

Prudent risk management, acumen to build on opportunities

For institutional investors and investment managers, a core principle of real estate investment is to create and sustain long-term value and, importantly, to avoid losses. Risks to investment performance arise from new regulatory frameworks and legal requirements, market shifts in occupier preferences and changing behaviour and the long-term risks that climate change, energy security and resource scarcity pose to their real estate investment. In light of the evidence, institutional investors must recognise that it is their fiduciary duty to understand and actively manage these risks today. Importantly, when it comes to sustainable real estate not all is a risk. The current market changes present numerous opportunities for investors to add value to their real estate investments.

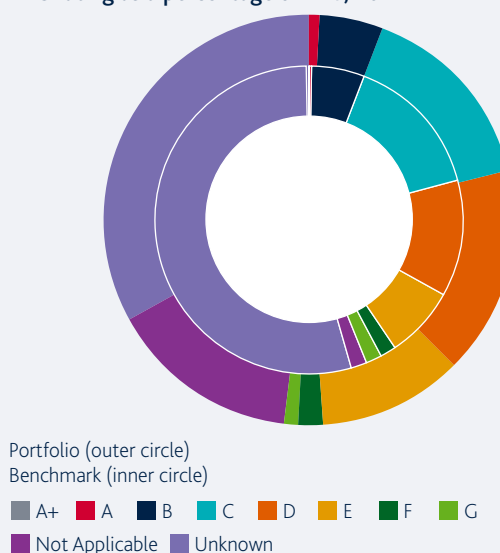
Over the last few years along with global institutional investors⁴, we have made the business case for investing in sustainable and energy efficient buildings based on the market fundamentals of real estate.

At the portfolio level, the first step required within the integration process is the assessment and understanding of sustainability regulatory and market risks and then subsequently to ensure that the management of these risks becomes part of the standard investment processes. At Hermes Real Estate we use the outcome of the risk assessment process to inform the portfolio investment strategy which is then integrated into our standard clients reporting.

Energy performance absolute and relative risk exposure

At Hermes Real Estate we carry out a regular regulatory risk assessment of our standing portfolio against European and UK medium- and long-term policy requirements. For example, in preparation for the UK new Minimum Energy Efficiency Standards (MEES) regulation, over the last few years we have been assessing the risks arising from our exposure to energy performance certificates (EPC) ratings. Based on the risks identified, on a fund by fund basis, we have built mitigation approaches into the investment strategies: improvements through refurbishment and planned maintenance, change of use, or sale.

EPC rating as a percentage of ERV, 2014



⁴IIGCC, March 2013: "Protecting value in real estate – Managing investment risks from climate change", www.iigcc.org/files/publication-files/IIGCC_Protecting_Value_in_Real_Estate.pdf

UNEP FI, February 2014: "Investor briefing, commercial real estate: Unlocking the energy efficiency retrofit investment opportunity", http://www.unepfi.org/fileadmin/documents/Commercial_Real_Estate.pdf

EEFIG, February 2015: "Energy Efficiency – the first fuel for the EU Economy: How to drive new finance for energy efficiency investments", www.eefig.com

Portfolio level

Investing responsibly



Future proofing

Acquisitions and transactions

It is important that sustainability risks within a portfolio are assessed at the acquisition stage. This is crucial to the early identification of mitigation actions ensuring that the portfolio is future proofed. We carry out a sustainability due diligence for new acquisitions for prospective assets. Working with our investment teams this enables us to identify cost effective environmental improvements required and impacts on refurbishment budgets. These risks are then integrated into our discounted cash flow analysis.

Acquisition due diligence and improvement plans

The market conditions in the last two years have led to a large number of acquisitions into existing funds and newly established funds. Overall, three of our newly acquired assets, Aldgate House, Finsbury Tower and Chiswick Tower accounted for over half of the total emissions from all the new assets. The risk assessment enabled us to identify this risk and mitigate it against the building characteristics and the investment plan for the asset. As a part of the investment survey, sustainability improvements were identified and integrated into the future investment plan for these assets, whether in refurbishment budgets or in the property management programme.

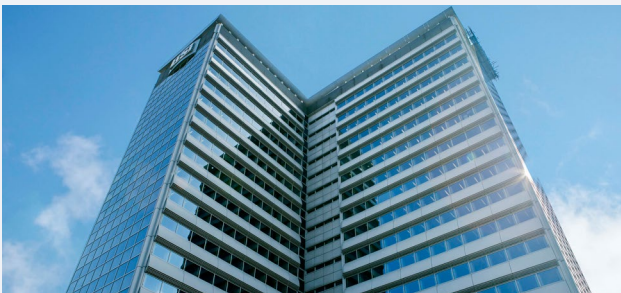


Image: Chiswick Tower, London. Newly acquired investment opportunity of 1960's bespoke office building in up and coming Chiswick next to extensive public transport. Provides good opportunities for value add through active management and progressive sustainable refurbishment.



Valuing sustainability

Spreading responsibility across practitioners

The responsibility for managing RPI risks in real estate investment has spread to a wide range of real estate practitioners. An important shift is the growing recognition of the role and responsibilities of valuers in integrating RPI considerations in their assessment of building investment values. The January 2014 edition of the Professional Valuation Standards by the Royal Institution of Chartered Surveyors (RICS), Red Book, now specifically lists sustainability as a factor that valuers need to take into account when performing valuations and risk assessments for their clients. Consequently, they are now advised to refer to sustainability metrics, as this will contribute to the level of information available.

In recognition of this, at Hermes Real Estate we have supported and contributed to a number of developments to further engage with valuers on sustainability. We took part in the development of the IPD/MSCI EcoPAS risk assessment tool. Consequently, when working with our valuers we now utilise this tool, in line with RICS valuation guidance, to collect and assess building sustainability characteristics. The results of the risk assessment are used to inform our asset management and portfolio strategy as well as valuation reviews.

Valuing sustainability in practice

- Development of sustainability questionnaires and benchmarks: EcoPAS risk assessment launched by International Property Databank (IPD, now MSCI) and the Royal Institution of Chartered Surveyors (RICS).
- Collaboration with valuers to collect sustainability data annually as part of standard valuation assessments.
- Working on discounted cash flow models taking account of sustainability metrics.
- Working with RICS to educate the sector, RenoValue project.



Sustainability benchmarks

Improving sustainability monitoring and benchmarking

Managing and monitoring of asset managers sustainability performance has become simpler and more transparent with the emergence and uptake of a large number of global and regional sustainability benchmarks and reporting guidelines. The Principles for Responsible Investment (PRI), for example, whose signatories professionally invested an estimated €5.6 trillion in real estate in Europe as of mid-2014⁵, provide a dedicated real estate reporting framework. The number of participants to the Global Real Estate Sustainability Benchmark (GRESB) meanwhile has increased exponentially over the last three years with the benchmark now covering over \$1.6 trillion in assets under management.

We have been active in developing a number of these tools and we make particular use of BBP Real Estate Environment Benchmark (REEB), IPD/MSCI EcoPAS and GRESB as each have a particular relevance in our investment process and respond to the need of a particular element of the investment cycle.

Sustainability benchmarks, different tools for different purposes

Different sector tools are adapted to specific needs of the investment cycle:

- **BBP Real Estate Environment Benchmark (REEB):** enables us to understand real operational performance year-on-year against annual industry comparison, which helps to identify action areas for improvements. Jointly with Hermes cost benefit analysis tools, it enables us to identify the most cost-effective improvements for a given asset and integrate this into the asset business plan in line with its investment life cycle.
- **IPD/MSCI EcoPAS:** enables us to benchmark the sustainability risks to which our real estate funds and portfolios are exposed in absolute basis and compared to our peers. The information gathered is used to inform Hermes Real Estate clients' strategies and is integrated into our risk assessments, fund business plans and investment decision making processes.
- **Global Real Estate Sustainability Benchmark (GRESB):** enables us to monitor our governance structure and sustainability performance of our real estate portfolios and report relative and absolute performance to our asset owners clients. When analysing peer performance we have found GRESB to be a useful road map to assess progress in the industry.

Hermes Real Estate awarded 4 GRESB Green Stars 2014

Sector leader for The centre:mk, 2nd amongst peers and 6th overall for Hermes Central London, 5th amongst peers for HPUT, 8th amongst peers for BTPS and tied 3rd amongst peers for BTPS development.



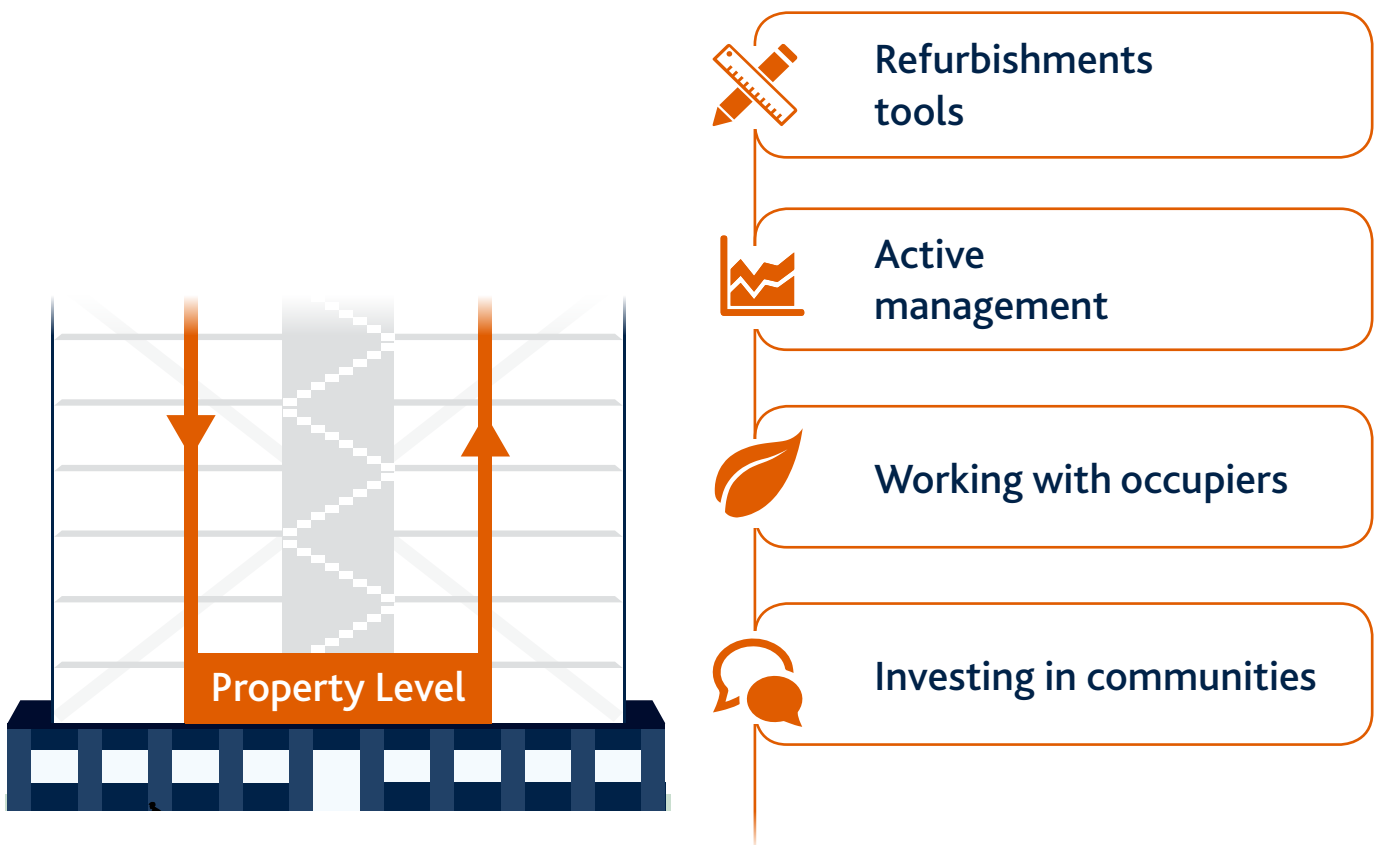
⁵ Monthly statistical bulletin, October 2014. Estimate of the total real estate market \$7.6 trillion in Europe, gathered from: EPRA (2014). Retrieved from: http://www.epra.com/media/Monthly_Statistical_Bulletin_October_2014_1414927075752.pdf

Property level Managing responsibly

At the asset level, the strategic view is that owner and occupier preferences for buildings with better environmental performance will lead to those assets experiencing higher net income growth due to lower depreciation and operational costs. A number of publications have shown that a correlation exists between more sustainable and energy-efficient buildings, higher rents and higher sale prices as well as between low-performing buildings, value decline and longer vacancy rates in various jurisdictions across the globe⁶.

Moreover, there are occupiers' benefits from green buildings. Green buildings with good air quality and high levels of daylight have been shown to reduce absenteeism, improve productivity and concentration, reduce stress levels and achieve an overall increase in user wellbeing. Such improvements have been proven to translate into financial benefits. The EU studies found that health benefits from energy efficiency improvements in buildings could be worth €40-80bn a year. A US study also found the potential benefits of improved indoor air quality and healthier workplaces to be worth US\$17-30bn a year, with additional savings of US\$20-60bn from improved employee productivity⁷.

On our directly managed funds, we implemented a comprehensive version of our RPI programme focusing on each of the investment phases of the building life cycle, with a particular focus on active management and illustrated in this section.



⁶ Principles for Responsible Investment, UNEP FI and UN Compact, September 2012: "The environmental and financial performance of buildings – A review of the literature".

⁷ www.annualreviews.org/doi/abs/10.1146/annurev.energy.25.1.537



Refurbishments

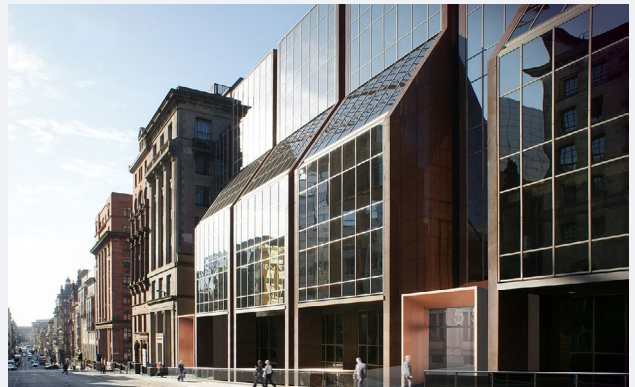
Improving the value and performance of legacy buildings

Improving the value and performance of legacy buildings has been a key part of the Hermes RPI strategy. As a result, we have tailored guides and minimum sustainability requirements for refurbishments and developments to capture environmental and health improvement potentials at this crucial step of the building life cycle.



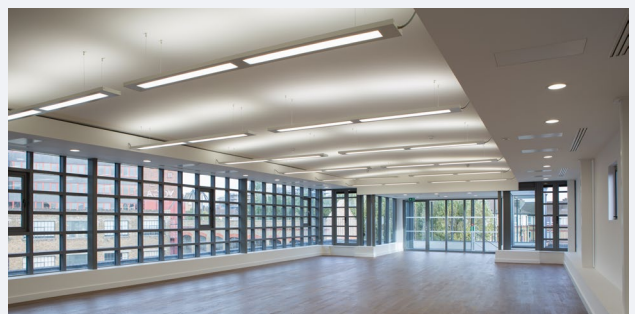
100 New Oxford Street, London, life cycle improvements

100 New Oxford Street was included for a number of years in our active management programme where it delivered continuous sustainability performance. From 2012 it has been refurbished in a multi-stage development, achieving BREEAM Very Good and an EPC of C. The asset has now been sold above market rates reflecting specifications matching market demand for this location near the new crossrail station.



151/155 St Vincent Street, Glasgow, RPI award 2012

In 2012, this 1980 eight-storey office building, underwent an extensive refurbishment while retaining the existing façade and achieved a very good BREEAM rating and an English EPC C rating. The refurbishment team delivered consistent RPI monitoring and reporting of progress over time. Environmental issues featured highly in the marketing material, displays and speeches at the successful marketing launch of the building. The refurbishment delivered a business space to match tenant demand in this market while following Hermes Real Estate RPI requirements. In 2014 the asset was sold above market rates reflecting specifications matching market demand for this location in Glasgow.



75 Bermondsey, London, sustainable refurbishment RPI award 2014

In 2014 the RPI award for Responsible Refurbishment went to 75 Bermondsey, which saw a complete refurbishment to a BREEAM Very Good rating and an EPC Rating of B. The value of this improved asset was immediately apparent as the entire building was quickly let to a single tenant, setting a local area rent record.

Property level

Managing responsibly



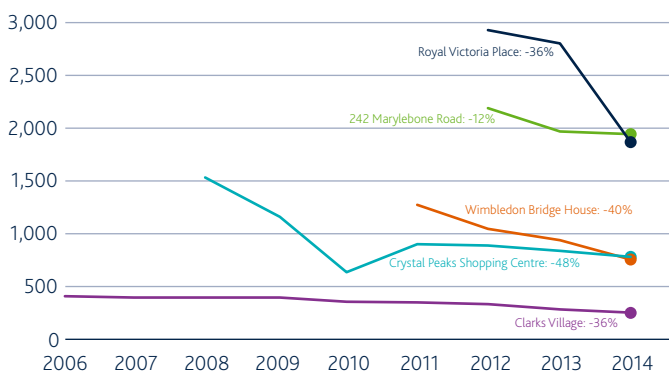
Active management

Positive impacts of responsible property management

We have integrated a sustainability management system into our property management processes. The system helps deliver minimum environmental performance requirements and targets. These are the responsibility of our asset managers and are set in the contracts of our property managers. As part of the process, the system delivers monthly and quarterly monitoring of performance with continuous feedback between property managers, asset managers and sustainability experts.

The specific case studies below demonstrate the effective implementation of an active management programme which reduces the operational cost of running these buildings whilst improving their quality. In 2010 and 2011 Hermes Real Estate acquired several energy intensive assets. Since acquisition, we have worked with the property managers to actively improve the efficiency and performance of these assets – which have been collectively reduced by more than 1000 tCO₂e or about 3% of our total carbon footprint per year by 2014.

Hermes' RPM Programme: Delivering Efficiency Savings Absolute Annual Carbon Emissions Under Hermes Management



242 Marylebone Road, London, RPI award winner 2014

An array of asset improvements include installing LEDs and microwave occupancy sensors in common areas to reduce electricity use and converting to waterless urinals. The latter achieved a saving in excess of 4,000 cubic metres of water per year, a 59% reduction in water use compared to the year before. Energy management has also played a vital role, optimising plant running times through incremental improvements and tenant engagement. In the two years since the property joined the Responsible Property Management programme, this site has achieved a 27% reduction in total energy use.



Wimbledon Bridge House, London, RPI award winner 2013

Numerous initiatives have been implemented that exemplify active management and ongoing improvement. Lighting Design High frequency T5 lamps and high frequency ballasts or LED (light emitting diode) fittings installed throughout building with presence sensor controlled lighting. Installation of low NO_x emitting boilers, central chilled water plant installed, phased replacement of chillers and boiler improvements. Improved management of building controls with heating and cooling independently controlled on a floor by floor basis and building management system serving the mechanical plant. Combined these initiatives have halved energy use annually and facilitated large emissions reductions over the years at this site.



2 Cavendish Square, London, EPC improvements

A historical building in the centre of London, over successive years of active management, preventive maintenance and floor by floor refurbishment we have delivered continuous improvement on environmental performance. Through dynamic EPC modelling and focused scenario analysis of potential energy efficiency improvements we have raised the EPC levels from originally a whole building rated G in 2008 to floor by floor ratings up to C and D ratings in 2014. Improvements were identified through a more precise assessment of the building's characteristics and dynamic modelling. They include boiler and chiller improvements, variable speed pumps, efficient and LED (Light emitting diode) lighting replacement.

Property level

Managing responsibly



Royal Victoria Place Shopping Centre, Tunbridge Wells, RPI award winner 2014

Moving from the worst performer in the BBP REEB benchmark when Hermes Real Estate acquired management control, an active management programme has turned around the energy performance of the asset. The energy management programme includes a large engagement programme reaching out to employees and tenants. This is coupled with a thorough review of all site equipment consuming energy and the 'turn off' campaign. It has resulted in an extensive initiative to decommission selected appliances or active management of other equipment to ensure appropriate utilisation patterns. This has delivered outstanding performance of over 36% energy consumption reduction. Using the savings achieved through the energy management programme, a staged LED roll-out programme was developed which maximised surplus funds from the energy budget.



Crystal Peaks Shopping Centre, Sheffield, RPI award winner 2013

The centre has achieved a 47% reduction in energy use since its peak in 2008. Active energy management and staff engagement has complemented a full scale LED roll out in common areas and the implementation of solar panels on site. The electricity generated is sold on site to the occupiers at discounted prices compared to their grid costs, ensuring they benefit from the scheme.

Clarks Village, from LEDs to PVs

Clarks Village installed LEDs across the car parks reducing landlord-consumed energy by 12%. The setting in Somerset optimises use of the installed solar panels, enabling a reduction in energy required from the grid, now 39% lower than the 2006 baseline demand.



Working with occupiers to enhance sustainability performance

Across our buildings we aim to establish a constructive dialogue with occupiers and have a number of engagement activities responding to their needs and strengthening the sustainability performance of our buildings. In addition we have introduced 'green' clauses in our standard lease since 2006. Negotiating the inclusion of these clauses can be a difficult task as there is still misunderstanding among occupiers on the motivation and associated risks behind them. However we have seen that negotiating these leases can also offer opportunities to strengthen the dialogue with occupiers. We monitor our success in negotiating these clauses and seek to use these as an engagement tool with our occupiers.

'Switch Off' at Royal Victoria Place

The property manager delivered a successful tenant engagement on 'Switch Off' and waste campaign, which led the centre to be awarded the BCSC Gold Award in 2014 and Hermes RPI award 2014.



Green leases negotiations on the up

Our lawyers at Hermes Freeport Outlet Portfolio managed to include green and CRC clauses in over 90% of the leases signed since April 2012 in Hermes Freeport Outlet portfolio. Through this action DAC Beachcroft, have demonstrated that given the right lease structure, it is possible to engage with retailers on this sensitive legal issue.



Image: Freeport Outlet Portfolio, DAC Beachcroft, RPI award 2014

Green leases success in mixed use portfolio

While on a mixed sector portfolio, including offices, industrial and retail, Nabarro – RPI awards 2012, have successfully delivered the inclusion of green clauses in over 45% of the leases signed since Feb 2012. Particular success includes Crystal Peaks, Christopher Place, Kelvin Way Estate and the Bermondsey properties.

Property level

Managing responsibly



Community

Investing in communities to build mutual value

Our community programmes and best practice tools aim to deliver social and community benefits, with a strong focus on skills and employment in line with local demand.

The centre:mk skills development programmes

The MK College Showcase has been a successful programme that allows recent arts, design and media students to showcase their work at the end of term, which counts towards the student's examination and final grade. This promotional opportunity resulted in work placements or sponsorship to continue development. The Young Enterprise Fair is an event for the UK's leading enterprise education charity. The aim of the event is to build a connected world of young people, business volunteers and educators, inspiring each other to succeed through enterprise.



Image: Skills development programmes, RPI award 2014

Love to help at Crystal Peaks

To celebrate the 25th anniversary of the centre the team pledged to support 25 local charities and organisations. After announcing this to the press there were over 60 submissions – 25 organisations were chosen, many of which were new to Crystal Peaks. The proviso: the organisations had to have a significant and meaningful specific impact upon the area within our primary and secondary catchment. The next stage was to meet with all 25 successful applicants and to draw up plans for how they could help throughout the year. They established whether the partners required financial assistance e.g. donation, fundraising or awareness raising or volunteer time. 18 of the 25 projects have been completed including The Sick Children's Trust, St Luke's Hospice, Whirlow Hall Farm, New Hope Food Bank, Birley Spa School Nature Area, Crystal Peaks Runners Sponsorship to name a few.



Image: Crystal Peaks, Sheffield, RPI award 2013

Offices' community programme

For offices, building community involvement can be more challenging. However, a joint programme for tenants at Camden Works and 242 Marylebone Road resulted in a gardening programme at a local London primary school where occupiers from the offices, led by professional gardeners, planted new garden areas. For the students, access to green spaces can be limited so this was a welcome improvement to their lives. For the occupiers who participated it was quoted that "it was nice to give something back" to the local community.



Image: Camden Works, London

King's Cross Academy

The new Academy draws upon the exceptional facilities being created at King's Cross, the expertise of the team behind the King's Cross regeneration project and the unique relationship with incoming occupiers to develop a first-class educational offer and enrichment programme. The King's Cross Academy Trust, approved by the DfE as a sponsor, is being formed by the King's Cross Central Limited Partnership and Michael and Clara Freeman who have a long standing commitment to support schools and universities. The Academy vision is of a school which keeps pace with our rapidly changing world and prepares children for the opportunities and challenges that will face them in the 21st Century. Driven by its motto 'Love learning together' it will promote an inclusive and respectful ethos that celebrates the richness and diversity of its location and population as well as promoting high aspirations and educational attainment. The new Academy opening in September 2015 will offer a unique opportunity to Camden Town children to make the most of their potential.



Image: King's Cross Academy, London

Property level

Managing responsibly



Active Management

Managing risk and safety performance

Hermes Real Estate is committed to providing safe working environments for those clients where we provide an asset management service. This commitment is for the benefit of all users, including our employees, our contractors, our tenants and their customers, visitors and members of the public. It is Hermes Real Estate policy, so far as is reasonably practicable, to:

- Provide and maintain a safe and healthy working environment through the appointment of competent staff, property managers and consultants;
- Appoint competent health & safety professional advisors as appropriate;
- Allocate sufficient resources to enable the health & safety policy to be effectively implemented;
- Regularly review our health & safety performance and engage all employees and partner organisations in this process to develop a culture of health & safety best practice.

While Hermes Real Estate has discharged direct management of health & safety and regulatory compliance requirement to contracted property managers it recognises it has a responsibility to ensure that these duties are being carried out in line with current legislative requirements. This is managed through monthly and quarterly review meetings and the appointment of appropriate competence advisors. In addition, the Health and Safety Steering Group reviews health & safety policy and activity across the Hermes Real Estate portfolio and monitors legislative changes which may impact on the discharge of health and safety management.

Fire strategy at Finsbury Tower

London Finsbury Tower, 103-105 Bunhill Row, is a 15-storey 150,000 sq ft tower in the City, purchased in August 2013. On acquisition, a full building fire risk assessment was carried out including the collation of tenant fire strategies. Fire systems maintenance and testing were brought up to date, improvements were identified and included in preventive maintenance plans.

In February 2015 there was a fire on the 8th floor of the building in the tenant premises. A full audit of the building was undertaken by the Fire Brigade which vindicated the improvements implemented. Evidence provided of the fire system review and of improvements to the practices and systems in the building led to conclusion that the systems were adequate. They ensured the fire was quickly addressed and the damages limited.

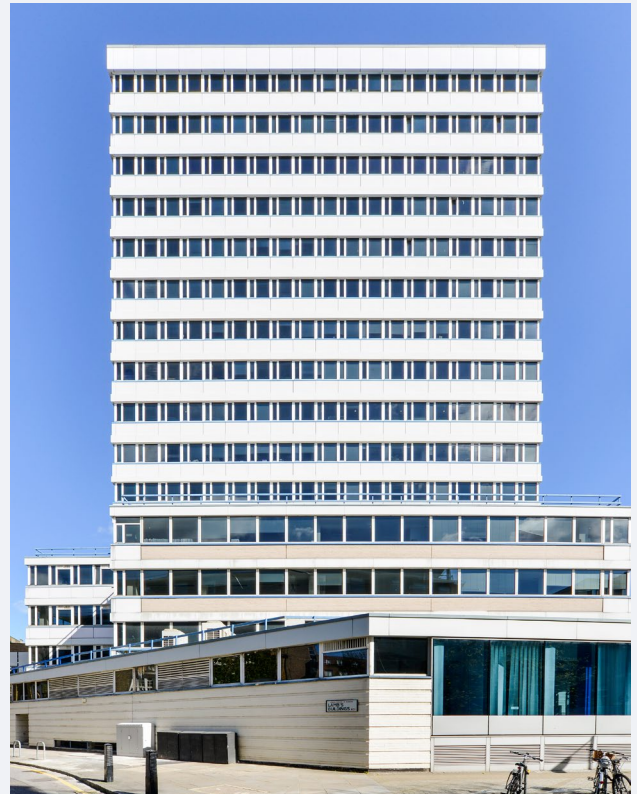


Image: Finsbury Tower, London

Delivering responsible performance

Targets⁸



↓ **40%**

reduction in absolute CO₂ emissions of standing portfolio by 2020 compared to 2006⁹



↓ **20%**

water consumption reduction by 2020 compared to 2006



↓ **5%**

reduction in emissions intensity of standing portfolio per year



↓ **5%**

reduction in absolute emission per year⁹ on a like-for-like basis



80%

on- and off-site waste recycling per year



92%

risk and safety improvement requirements completed on time¹⁰

Financial savings

Energy savings from our property management activities

2014: **£600k**

Averted direct landfill tax from all managed waste

2014: **£880k**

Risk and safety performance

88%

risk and safety improvement requirements completed on time

⁸ Targets cannot be guaranteed.

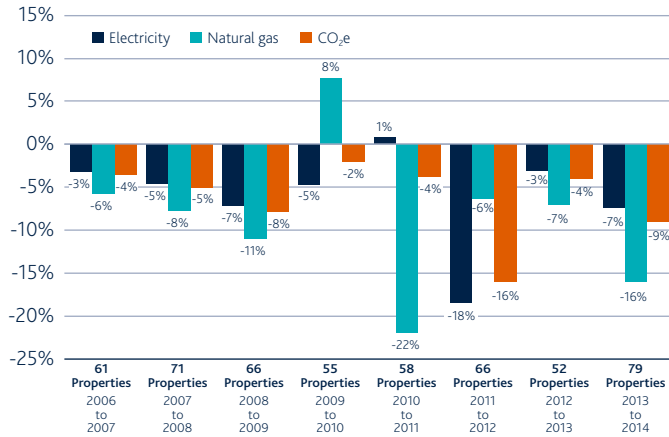
⁹ Where we have the ability to delineate between owner and occupier's areas, we report on owner data only, where this is not possible we have included occupier's data.

¹⁰ In 2015 we have reviewed Hermes Real Estate risk and safety systems and updated our methodology to monitor and report performance and revised our target accordingly.

Environmental Performance

Active management

Annual change in carbon emissions on a like-for-like basis for eight rolling quarters adjusted for heating degree days (%)



8

Straight years with like-for-like emissions reductions



9%

emissions reductions across the like-for-like portfolio



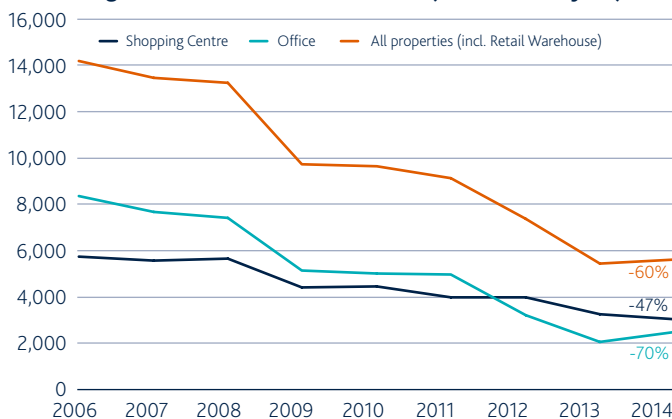
6.4%

the average emissions reduction per year over the past 8 years

Since the baseline year eight years ago in 2006, every year Hermes' like-for-like portfolio achieves reductions in emissions, an average of 6.4% per year. This year in particular, the like-for-like portfolio has seen a 9% reduction, in spite of a sharp increase in the electricity emissions factor relative to the year before. The reduction comes from a general trend across the portfolio of energy management and improvements with stand-out performances at Royal Victoria Place (-41%), Wimbledon Bridge House (-27%) and 242 Marylebone Road (-12%) in 2014.

Active management & refurbishments

Changes in absolute landlord controlled carbon emissions for the 18 buildings held between 2006 and 2014 (tonnes CO₂e/year)



18

Buildings since 2006



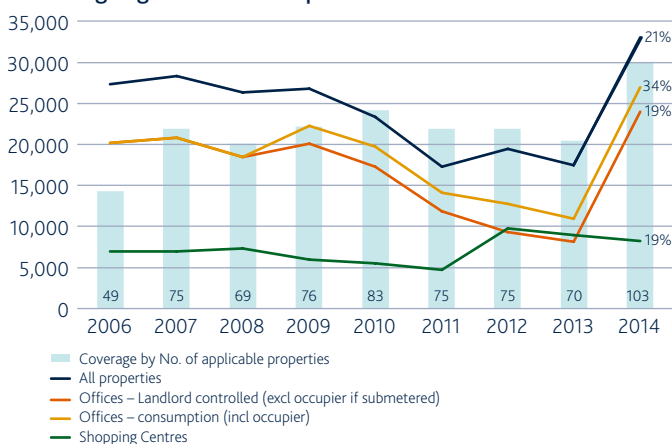
60%

reduction since 2006

18 buildings remain in the portfolio that were included in the baseline year in 2006. After eight years of Responsible Property Management, Hermes' there has been a 60% reduction in emissions for these assets. These reductions are due to good management, refurbishment of some assets and improvement in metering attribution. For example, 100 New Oxford St has achieved a reduction of over 65% since 2006 in electricity use.

Transactions, management and refurbishments

Changes in absolute carbon emissions for landlord controlled standing portfolio between 2006 and 2014 (tonnes CO₂e/year)
Percentage figures below compare 2014 with 2006 Baseline



↑

21%

absolute increase against baseline

↑

30%

increase due to 20 new assets added to the portfolio in 2014

↑

11%

increase in emission factor of UK electricity grid in 2014

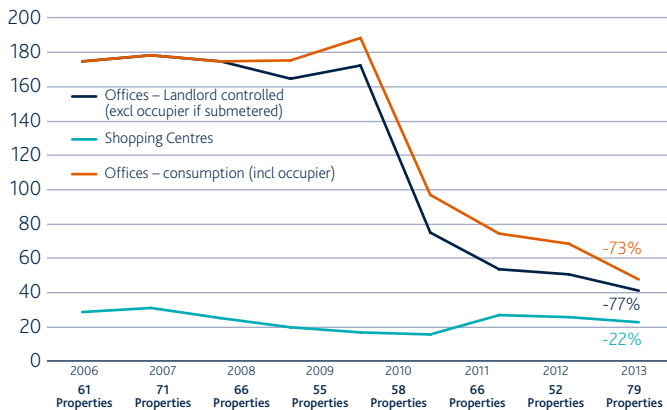
Acquisitions of 11 large and energy intensive offices and the introduction of our new Metro PUT portfolio has increased the absolute emissions by almost one third. The top 3 emitting newly acquired assets, Aldgate House, Finsbury Tower and Chiswick Tower account for over half of the new emissions. Offices now account for 64% of overall portfolio emissions, compared with 34% for Shopping Centres. Other retail and industrial account for 2%.

In 2014 the official Defra emissions factor for grid electricity in the UK increased by 11%, which also has played a significant role in the increase in emissions reported for the year.

Environmental Performance

Transactions, management and refurbishments

Changes in energy intensity for like-for-like portfolio of shopping centres & offices between 2006 and 2014 (kg CO₂e/m²/year)
Percentage figures below compare 2014 with 2006 Baseline



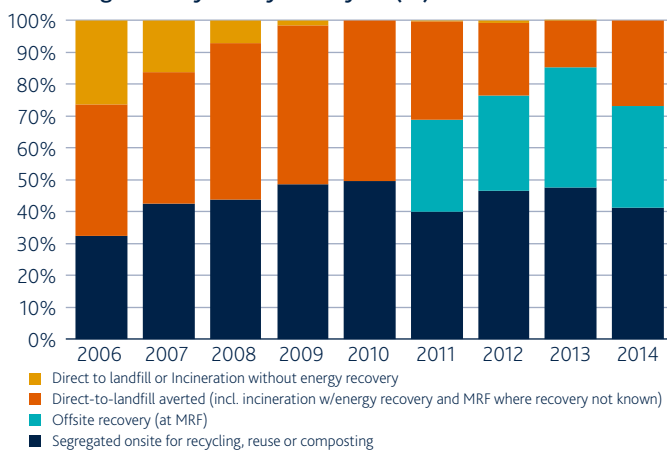
↓ **77%**
Offices since 2006

↓ **22%**
Shopping centres since 2006

Hermes energy intensity metric adjusted to lettable area highlights the changes in efficiency on site and is a useful tool for managing assets. This approach aligns to the metrics used in the BBP REEB benchmark. The major improvements have been achieved through the joint impact of our new transactions, active management, and refurbishments since 2006.

Active management

Proportion of waste by disposal route for standing portfolio measuring waste by mass year on year (%)



40%
Recycled, re-used or composted on site

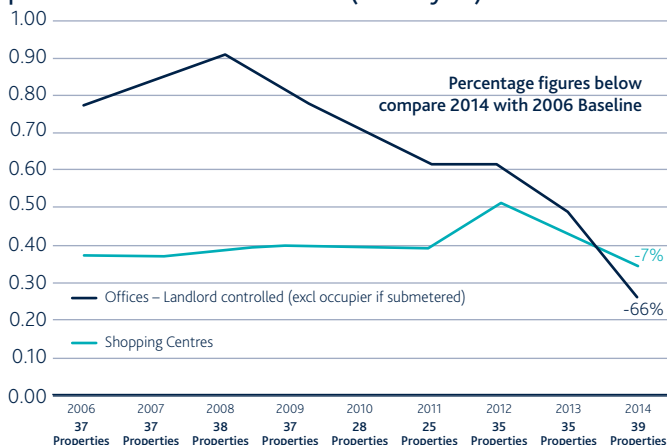
31%
Recycling off site (MRF)

29%
Incineration with energy recovery and MRF unknown

On and off-site recycling has slipped to below the target this year. This is in part due to average recycling rate of Materials Recycling Facilities which has gone down and an increase in use of incineration with energy recovery across the portfolio. It is also due to changes in the portfolio and newer assets where waste management schemes still need to be developed further. There is a growth this year in schemes that compost waste, at both Cheapside House and Abbey Gardens a food waste scheme has been implemented for the office and retail occupiers, and there is a similar scheme at Aldgate House.

Active management

Changes in water intensity for landlord controlled like-for-like portfolio between 2006 and 2014 (m³/m²/year)



↓ **66%**
Offices since 2006

↓ **7%**
Shopping centres since 2006

Water use in offices may have increased by 25% in 2014, due to the acquisition of new assets, but water intensity for offices has dropped by 38%. That is due to active management successes at sites like 242 Marylebone Road, where water has reduced to about one quarter the consumption of 2012, and half of last year. For retail, there is remarkable improvement again in 2014, with water intensity continuing to fall by 18% in 2014 after 17% the previous year.

Hermes Investment Management

Hermes Investment Management is focused on delivering superior, sustainable, risk-adjusted returns – responsibly.

Hermes aims to deliver long-term outperformance through active management. Our investment professionals manage equity, fixed income, real estate and alternative portfolios on behalf of a global clientele of institutions and wholesale investors. We are also one of the market leaders in responsible investment advisory services.

Our investment solutions include:

Private markets

International Real Estate, Pooled funds, Segregated mandates, UK Real Estate, UK Real Estate Debt, Infrastructure, Private Equity.

High active share equities

Asia, Global Emerging Markets, Greater China, Europe, Global and Small & Mid Cap.

Why Hermes Real Estate?

Hermes Real Estate is one of the largest real estate investment managers in the UK, with over £7.0bn Gross Asset Value (GAV)¹ of assets under management in both UK and International portfolios. It offers client-focused, property investment solutions through segregated and pooled structures.

¹ Hermes Real Estate as at 31 March 2015, £6.4bn NAV

Specialist fixed income

Global High Yield Bonds, Multi Strategy Credit, UK Government Bonds and UK & Global Inflation-Linked Bonds.

Multi asset

Multi Asset Inflation.

Responsible Investment Services

Corporate Engagement, Intelligent Voting, Public Policy Engagement and PRI.

Offices

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The value of the property is a matter of a valuer's opinion rather than fact.

All figures, unless otherwise indicated, are sourced from Hermes. For more information please read any relevant Offering Documents or contact Hermes.

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