INFORMATION FOR INVESTMENT PROFESSIONALS

Your success. Our priority.

Riding Europe’s building renovation wave

European equities | December 2020

Andrea Carzana
Portfolio Manager

Natalia Luna
Senior Thematic Investment Analyst, Responsible Investment

The EU’s decision to put building modernisation at the heart of its drive to reduce CO2 emissions heralds a major spending programme to transform energy efficiency. It also represents a wider drive across the continent in which Columbia Threadneedle is keen to be involved

The European Union is about to begin an ambitious programme that aims to improve energy efficiency in public and residential buildings throughout the continent. Over the next decade it looks set to create a wave of opportunities for investors across sectors from heating and cooling manufacturers to suppliers of insulation materials.

Unveiled this summer, the EU's Recovery package[1] has highlighted buildings as a key sector for investment as the bloc looks to ways to help offset the negative economic impact of Covid-19 and simultaneously deliver a green transition. Further impetus has come from the EU's ambitious Renovation Wave Strategy, launched in October, which aims to turbo boost decarbonisation initiatives, in part through the renovation of buildings.

As the EU looks to hit its self-imposed targets to reduce CO2 levels by 55% by 2030 (compared to 1990 levels) and reach net zero by 2050, policymakers have realised the need for radical action that goes beyond the energy sector. The renovation and retrofitting of buildings could play an important role: buildings account for more than a third of the EU’s greenhouse gas emissions (36%) and around 40% of total energy consumption. From the EU buildings stock of around 220 million units, about three-quarters are currently deemed energy inefficient.

In addition to possible EU-wide funding, it is also likely that some member states will develop their own national renovation plans, with some governments offering financial incentives to encourage renovation of private and residential buildings.

[1] All data in this article is included here unless otherwise stated: https://ec.europa.eu/energy/sites/ener/files/eu_renovation_wave_strategy.pdf

Investors should take note, as the positive implications of this investment drive have yet to be fully reflected in stock prices. This anticipated large scale of public policy initiatives and incentives, combined with significant public money, is likely to result in sizeable investment flows into building renovations, with a focus on heating, cooling and insulation. It is likely there will be corresponding share price gains for some companies operating in these sectors.

A long-term structural theme

The EU's targets are far-reaching. By 2030, the bloc is looking to cut the greenhouse gas emissions of buildings by 60% and reduce the energy consumed during heating and cooling by 18%. To help achieve this it wants to double the renovation rates of buildings from 1% to 2% annually within the next 10 years, ensuring that these renovations lead to improved energy and resource efficiency in around 35 million buildings.

Naturally, the drive for renovation commands strong political support. In addition to helping meet carbon emission reduction targets, the strategy is expected to boost economic growth, create jobs and deliver social benefits in the form of lower energy bills, particularly for poorer households.

The investment required will be significant. While specific funding has yet to be defined, the EU has identified that around €275 billion of investment annually will be needed. We expect the capital to come from a combination of public funding and private investment, encouraged by tax incentives and other public policy initiatives.

In terms of policy measures there are a lot in the pipeline. By the end of 2021, the European Commission will propose new mandatory minimum energy performance standards as part of the revision of the Energy Performance of Buildings Directive (EPBD). It is also set to update the framework for Energy Performance Certificates (EPCs) as it seeks to widen their coverage across member states. There is room for improvement, as in several member states EPCs cover less than 10% of the building stock. Stricter buildings requirements could be a strong catalyst in attracting large private investments into this theme.

Pricing in stock opportunities

While most of the regulatory push will come in 2021, it is likely that the market will start pricing in the opportunities for stocks ahead of these legislation changes. As the EU will prioritise funds for public buildings such as schools, universities and hospitals first, the companies with sizeable market share in these areas should logically benefit the earliest. Notably, the stocks of leading suppliers of insulation products seem likely to prosper.

The EU is fully committed to hit its climate change targets and has now put buildings renovation at the heart of them. In the years to come, this will prove a major structural policy-driven theme. Currently it is just getting started, and Europe’s equity markets have yet to reflect its consequences in the affected companies’ stock prices.

European sustainable outcomes and Columbia Threadneedle

Sustainable investing is a key focus area for Columbia Threadneedle, while the level of interest from clients continues to grow: globally, ESG and sustainable funds are seeing increased flows – in the US $10.5 billion was invested in sustainable funds in Q1 2020[2], and in Europe that figure was €30 billion[3].

With that in mind we have developed the Sustainable Outcomes Pan-European Equity strategy, which will complement our existing sustainable outcome equity offerings, Global Sustainable Outcomes and the Threadneedle UK Sustainable Equity strategy.

The Pan-European Equity strategy aims to invest in companies that not only do things right, but also do the right things – we believe doing well in business and doing good for the world need not be mutually exclusive. This philosophy is underpinned by an active approach to monitoring and regular engagement with companies' management and directors

The strategy will be managed by Andrea Carzana, and he will be supported by a European equities team of 23 financial professionals[4]. Also integral to how the strategy will operate is the work of the Global Responsible Investment research team, in which Natalia Luna will be a key contact. The RI team is a highly knowledgeable and dedicated team of 16 people[5], and its analysts' thematic work directly aligns with the strategy's sustainable outcomes framework. The ongoing data science development work around sustainable outcomes that the RI team undertakes will be an invaluable source of ongoing information.

---

[2] https://www.cnbc.com/2020/06/07/sustainable-investing-is-set-to-surge-in-the-wake-of-the-coronavirus-pandemic.html

[3] https://esgclarity.com/european-esg-funds-see-e30bn-inflows-in-q1-despite-covid-19-panic/

[4] As at 31 October 2020

[5] As at 31 October 2020