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Where investment makes a difference

# ‘The momentum is on the side of the transition’

Richard Craddock explains why Redevco is expanding into real estate credit with a focus on sustainability.

By Richard Betts

**R**edevco has been expanding into real estate credit. It is a new diversification strategy for the pan-European real estate investment and management company. *Impact* spoke to Richard Craddock, head of real estate debt, about the rationale for the new venture and its sustainability credentials.

## What is the underlying strategy?

The primary objectives for the launch of a private credit arm are twofold. First, to diversify our asset base for our balance sheet commitments. Adding debt gives us diversification of risk and income across our real estate investments. For our proprietary capital, it offers a greater balance and lower cyclicality. That diversification component is a key feature for us. The second objective is having greater product optionality for third-party co-investment partners. As part of our ambition to build a third-party investment management platform as well as use our own balance sheet, establishing a debt business gives us and our co-investment partners access to the opportunity we are seeing in the debt markets.

## How big a focus is sustainability?

Sustainability is a key focus for Redevco across all our investment strategies. The debt product is consistent with that approach and builds on that core skillset and understanding. Broadly speaking, we’re lending against two types of borrower business plans. The first is transitional assets, providing acquisition plus capex funding to retrofit standing buildings and decarbonise them. The capex funding will

go towards improvements to the physical space to drive leasing performance, but it will also include improvements intended to drive energy efficiency and to put them on a pathway to net zero. The second type of lending is ground-up construction lending to build future-aligned, sustainable properties. There will be a mix of the two options and we will remain cognisant of the embodied carbon impact of new builds.

There are three reasons for our sustainability focus. First, quite simply, it is the right thing to do and is consistent with what we already do on the equity side of the business. Redevco has ambitious net-zero targets and we’re investing heavily in the assets we own.

The second reason is that we think it is the most interesting part of the lending market from a relative return and value perspective. On the supply side, banks are increasingly hamstrung by regulations, which is restricting construction lending and refurbishment lending in particular. Whereas on the demand side, we are now five years away from 2030 Paris objectives, which is only one investment cycle away. There are binary regulatory deadlines related to energy and carbon performance across European markets that are getting ever closer, and even if some may be pushed back, this is still going to drive capital flows towards retrofitting.

The momentum is on the side of the transition so it is a question of when, not if. That demand for capital – a lot of which will have to come from the debt markets – will only accelerate as we near those deadlines, and that creates a really interesting dynamic for private credit to grow market

share and capitalise on the opportunities.

We see the transition as a generational opportunity. Redevco can use its own capital to meaningfully co-invest alongside third-party capital partners.

The third reason relates to optimising the downside risk in our loans. We think the risk profile for newly refurbished or constructed assets is preferable to being exposed to residual income on investment loans against assets at risk of obsolescence. Coupled with that, the returns available are outsized. Tenant demand for more sustainable assets is demonstrable. Corporate and residential occupiers and owners are increasingly carbon-conscious. Physical space that aligns with a company’s net-zero objectives is increasingly in demand and that’s driving occupational performance and rents.

Investing in these in-demand buildings is the most attractive risk we see. Clearly you take the risk on execution of the refurbishment or construction, but we are very experienced developers, so that is a risk we can underwrite and price, and we can use that knowledge to gain a competitive advantage.

## Are you targeting specific sectors and markets?

We look across sectors, as long as the underlying business plans are consistent with our sustainable focus. That will include well-located offices in gateway cities and we are seeing a lot of interesting opportunities there. We are also definitely targeting the living sectors, including build-to-rent, build-to-sell and operational sectors, like hospitality and senior living.



▲ **Hollandse Meesters in greater Amsterdam area: only WELL for residential project in the Netherlands, prioritising sustainability, health, wellbeing and comfort for its future residents**



**‘Physical space that aligns with a company’s net-zero objectives is increasingly in demand and that’s driving occupational performance and rents.’**

**Richard Craddock, Redevo**

We’ll focus on the mid-market products for residential, rather than the luxury end of the market where depth of demand is harder to underwrite and the social impact is lower. We will also support logistics, more likely from a ground-up construction perspective, but we will also consider refurbishments.

Alongside the more mainstream sectors we will look at operational real estate and alternatives. As for markets, we are pan-European and will consider all major Western European jurisdictions, including the UK, the Nordics and Iberia, where we have a strong presence on the ground.

### **What are the criteria for a development or retrofit loan?**

We have a framework in place that allows us to determine if a scheme is sufficiently aligned in its sustainability targets. It varies depending on whether it’s a refurbishment or a development. We want to lead the market when it comes to sustainable lending, so we drill down deeper into operational and embodied carbon performance rather than necessarily just relying on sustainability ratings, though they clearly offer a barometer. We adopt a partnership approach with borrowers to

support their business plans and appreciate that returns need to make sense against capex budgets. It needs to be asset-specific, there is no ‘one-size fits all’.

It also depends on how ‘brown’ a particular asset is at the outset of a business plan. Taking a very energy-inefficient building and bringing it to EPC B, for example, is a material improvement in getting an asset on a pathway, even if it’s not going to hit EPC A. When delivering a project we look at carbon, but we also take a wider view, taking into account biodiversity, social impact and other factors. Our main focus is on decarbonisation though, improving operational efficiency and minimising embodied carbon. The rest is important, of course, but for the time being decarbonisation will be our primary focus.

We work with borrowers and are very relationship focused. Increasingly, the institutional investor universe is aligned in terms of what they are looking to deliver from a sustainability perspective, particularly as we see the continued emergence of article 8 and 9-aligned funds under SFDR.

### **What about loan sizes and terms?**

We are flexible on loan sizes and will

start at around €15 million. Most of our transactions will be on three- to five-year loan terms, reflecting the hold period/ business plans of our borrowers.

We can be flexible on currency and will look at both fixed and floating rate loans. From a leverage perspective, we will average around 65% loan to cost, but we can go beyond this if we have a strong conviction. We provide mezzanine and senior loans, depending on the type of transaction.

We’re in the process of closing transactions already, which is really encouraging. We are seeing a lot of opportunities in the market from a great network of target borrowers and believe this is a strong point in the cycle to be commencing deployment.

Our focus is on supporting decarbonisation, but we’re a for-profit organisation with the downside protections that debt investing provides. The focus on return and sustainability are not mutually exclusive. We want to mobilise private capital to effect meaningful change and deliver consistently strong returns for both our balance sheet and our co-investment partners. The forces of capitalism will have to play an integral role if we are to affect the transition. ■



Rue de Rivoli in Paris, France

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