

# Adjustment of corporate real estate during a period of significant business change

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# Adjustment of Corporate Real Estate During a Period of Significant Business Change

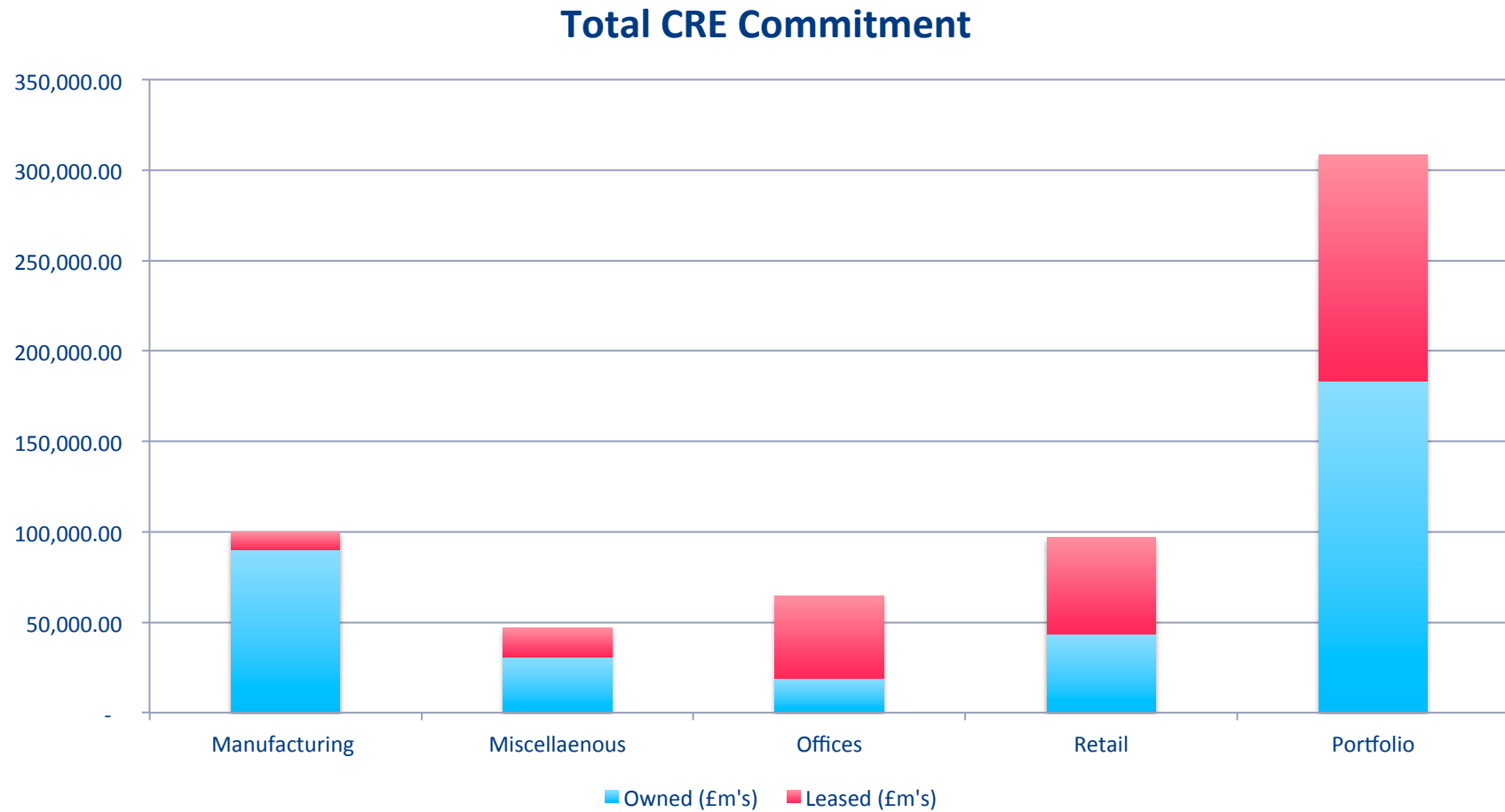
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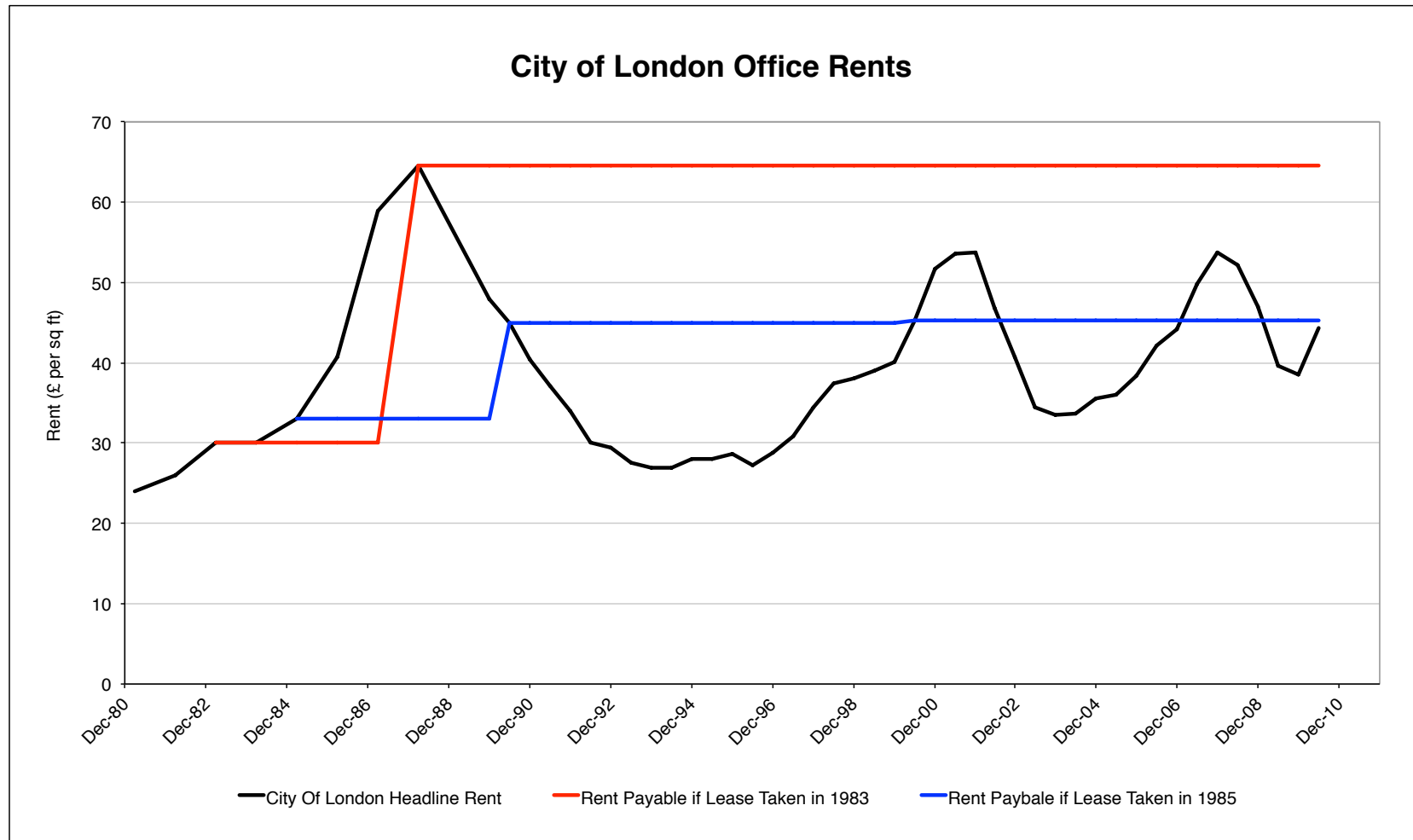
## INTRODUCTION

- *Sustained Competitive Advantage* (Porter 1985) – Managers look to improve Value Chain through efficiency, effectiveness and productivity
- Business environment continually changing. Has evolved to:
  - *Transient Competitive Advantage* (McGarth 2013)
  - *Blue Ocean Strategies* (Kim & Margborne 2015)
- Business now has to be agile, dynamic and flexible, capable of quickly adjusting to grasp opportunities
- Dynamic strategic fit requires a learning mind set and iterative feedback loops for the individual and organisation
- CRE Portfolio has to be agile, dynamic, and flexible, therefore, capable of quickly adjusting to changed business needs.

## RELEVANCE – SCALE OF COMMITMENT



## RELEVANCE – EXAMPLE OF ISSUE



## PROBLEM STATEMENT

- To meet today's challenges a business needs a flexible CRE portfolio capable of *Dynamic Alignment*
- Performance measures provide assessment base for business – both financial and CRE
- Performance measures linking business and CRE are Efficiency, Effectiveness, Productivity and Flexibility (Van Ree 2002)
- Flexibility can be defined as: Physical, Functional, Financial (Gibson 2000) and Legal
- Has business learnt from the past and built a CRE portfolio that facilitates Efficiency, Effectiveness, Productivity and Flexibility?

## HYPOTHESES

**H1:** Over time the length of commitment to leased property will reduce to reflect improved CRE flexibility and effectiveness of CRE use

**H2:** As turnover and profitability decline/increase management will react by reducing/increasing the proportion of total costs committed to CRE

**H3:** As the number of FTE's increases or decreases there will be a corresponding change to the CRE portfolio



## METHODOLOGY

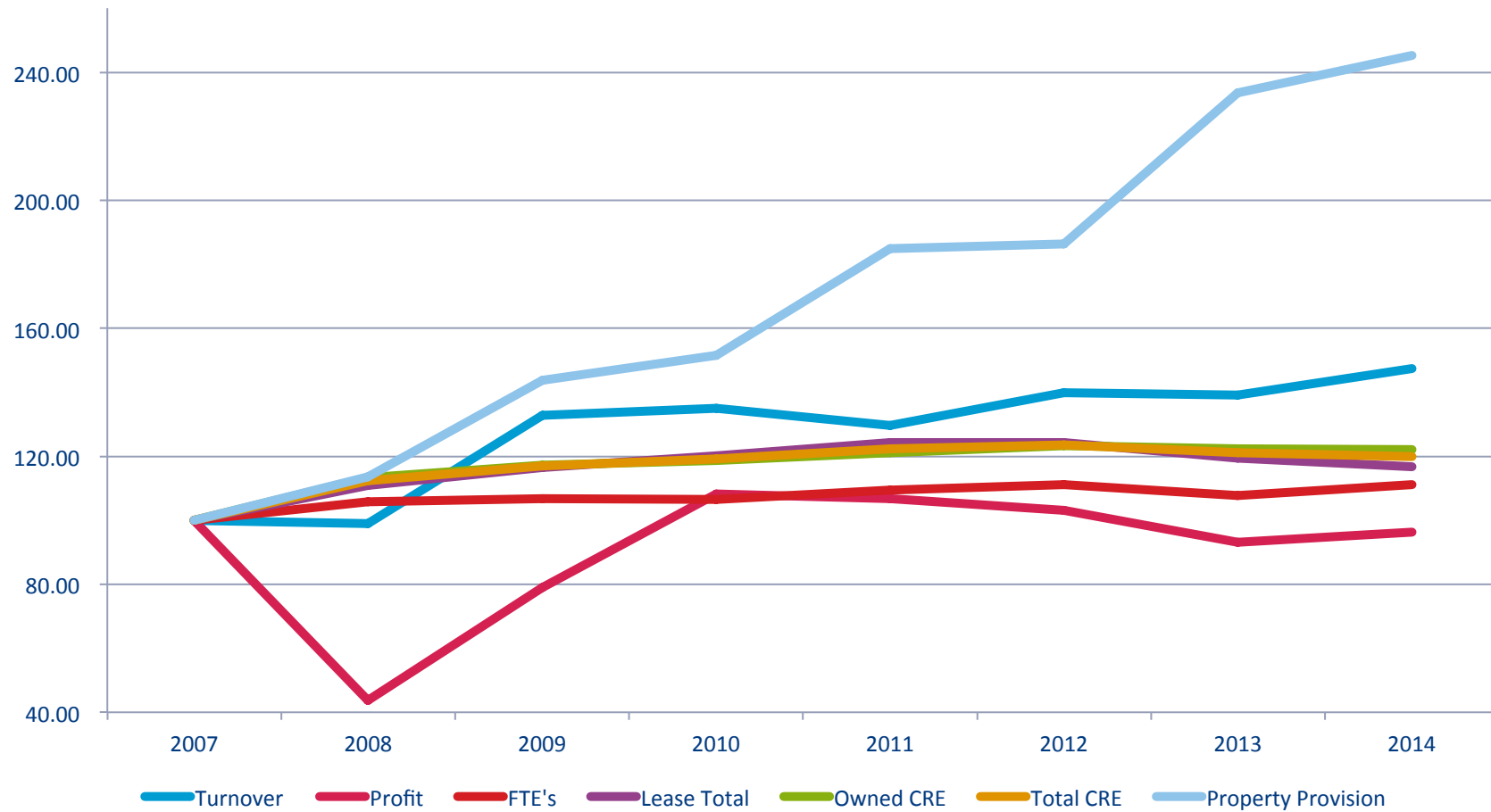
- Accounts 230 companies in the FTSE350 (2007 to 2014) analysed.
- Financial and CRE data extracted and grouped –
  - Offices
  - Manufacturing
  - Miscellaneous
  - Retail
  - All Companies.
- Descriptive analysis of sectors to provide overview
- Distributed time lagged auto regression model:
  - 1 year lag
  - Stepwise adding in of independent variables
  - 95% confidence limits

## MEAN VALUES PER COMPANY

MEASURE	VALUE	CHANGE 2007 - 2014	MEASURE	VALUE	CHANGE 2007 - 2014
<b>ALL COMPANIES</b>	230 Companies				
Turnover	£5,522m	47%	Freehold Value	£797m	22%
Profit	£475m	-4%	Property Provision	£17m	145%
FTE's	27,842	11%	Lease Total	£544m	17%
<b>OFFICES</b>	108 Companies: Finance (39); Construction (15); Professional & Support Services (29); Technology, Media & Telecommunications (25)				
Turnover	£5,575m	34%	Freehold Value	£177m	-4%
Profit	£486m	-12%	Property Provision	£25m	150%
FTE's	30,944	11%	Lease Total	£420m	4%
<b>MANUFACTURING</b>	54 Companies: Consumer Goods (15); Engineering (26); Industrials (13)				
Turnover	£3,730m	48%	Freehold Value	£1,666m	28%
Profit	£514m	51%	Property Provision	£3m	200%
FTE's	18,768	8%	Lease Total	£189m	41%
<b>MISCELLANEOUS</b>	45 Companies: Health (12); Leisure (8); Transport (8); Utilities (7)				
Turnover	£6,579m	95%	Freehold Value	£687m	9%
Profit	£465m	-28%	Property Provision	£6m	133%
FTE's	22,755	13%	Lease Total	£354m	18%
<b>RETAIL</b>	23 Companies				
Turnover	£7,417 m	36%	Freehold Value	£1,888m	39%
Profit	£345.m	-1%	Property Provision	£40m	135%
FTE's	45,268	13%	Lease Total	£2,330	26%

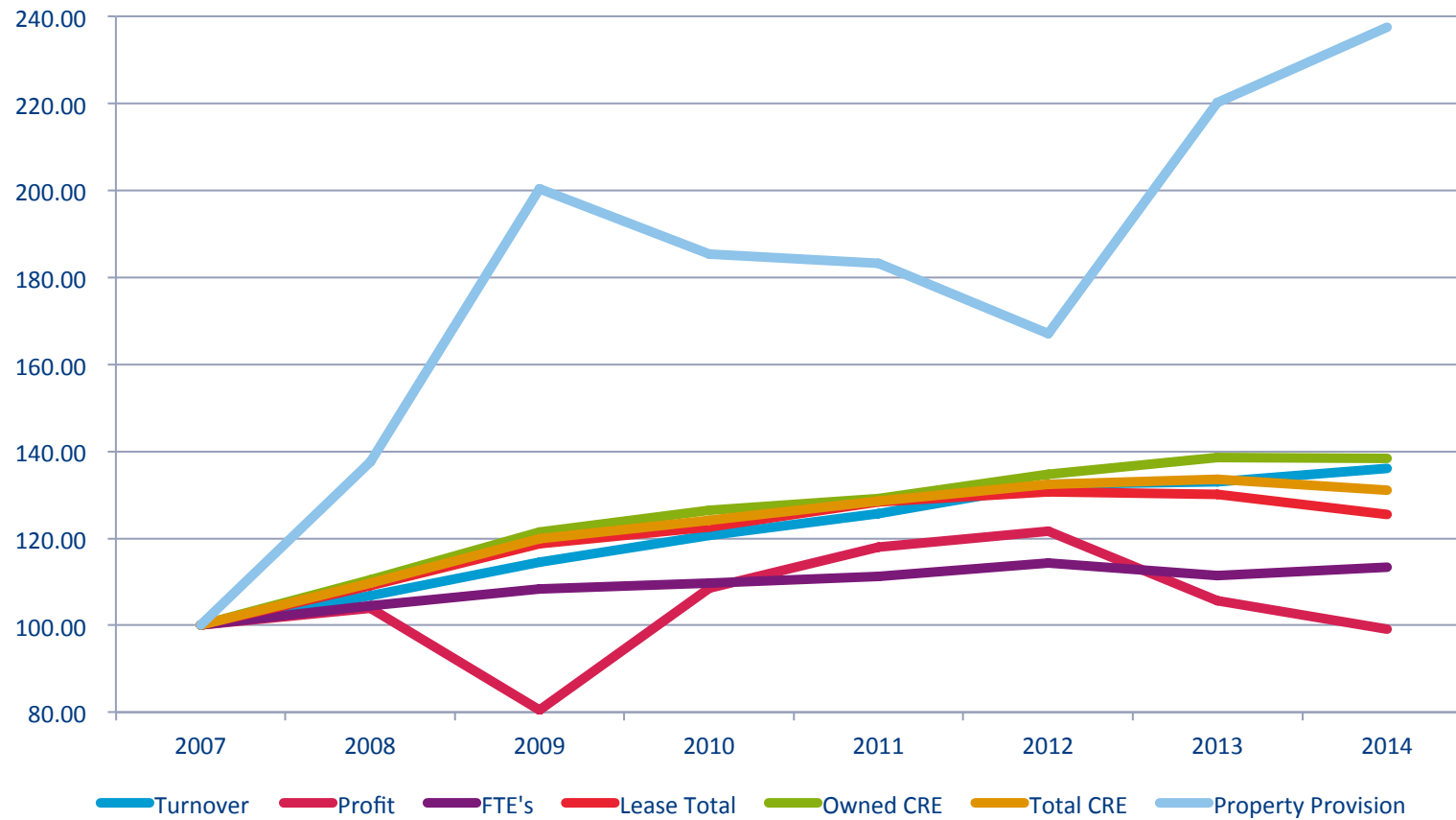
## PROFILE

### ALL COMPANIES



## PROFILE

### RETAIL

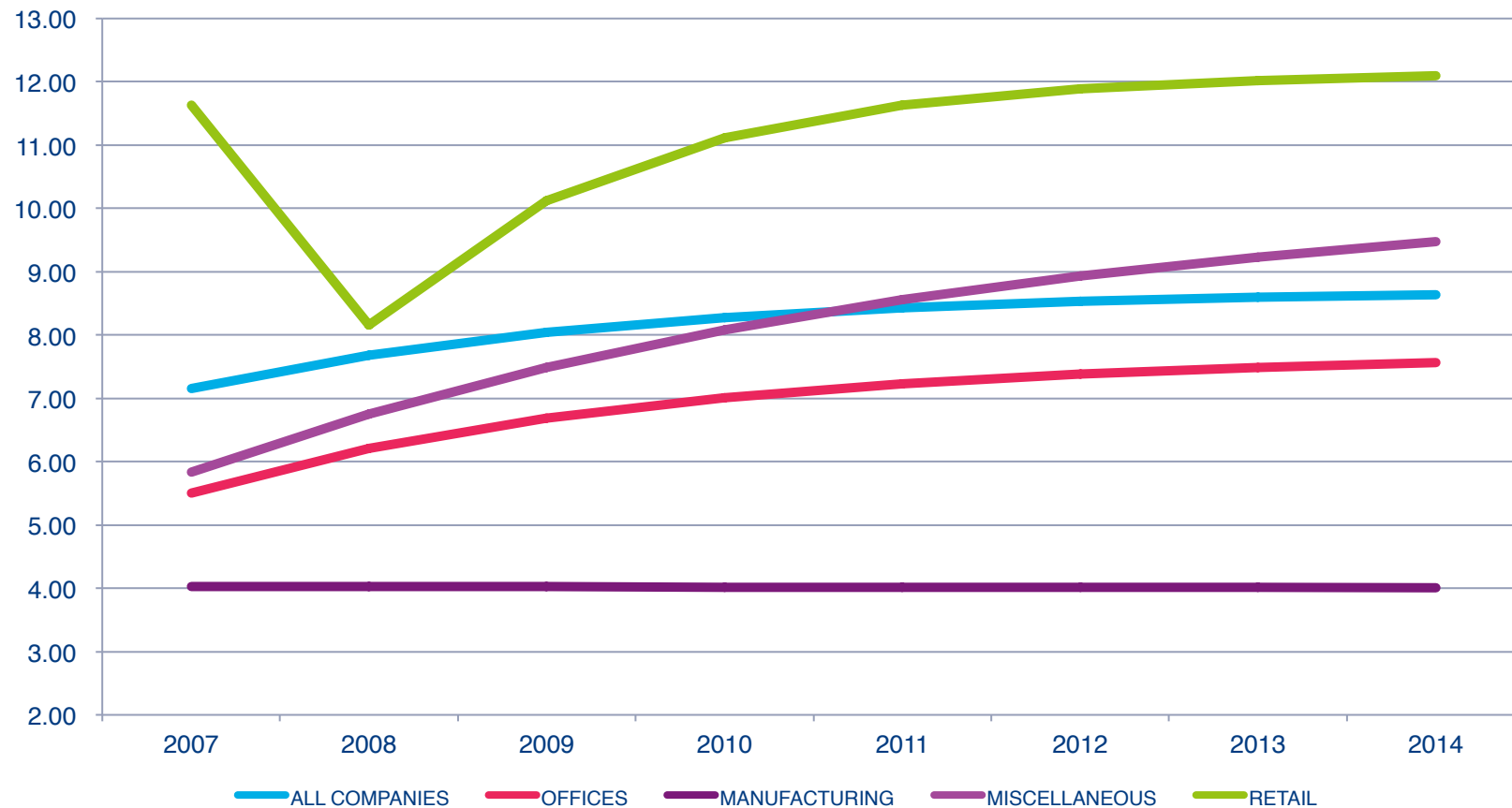


## H1: REGRESSION ANALYSIS: LEASES OVER 5 YEARS WILL FALL

<b>RETAIL - AVERAGE LEASE TERM OVER 5 YEARS</b>	<b>Estimate (Unstandardized Beta)</b>	<b>t-value</b>	<b>p-value</b>	<b>R<sup>2</sup></b>	<b>Adju. R<sup>2</sup></b>	<b>Sig. F Change</b>
				0.731	0.728	0.035
(Constant)	5.960	7.971	-0.0			
Previous Lease Term Over 5 Years	0.510	20.717	0.0			
Dummy2	-3.738	-2.123	0.035			
<b>RETAIL - OWNED CRE</b>				0.995	0.995	0.0
(Constant)	10.370	0.402	0.688			
Previous Year Owned CRE	1.039	183.594	0.0			
<b>RETAIL - TOTAL CRE COST</b>				0.992	0.992	0.0
(Constant)	-48.125	-0.802	0.424			
Previous Year Total CRE	1.049	142.609	0.0			

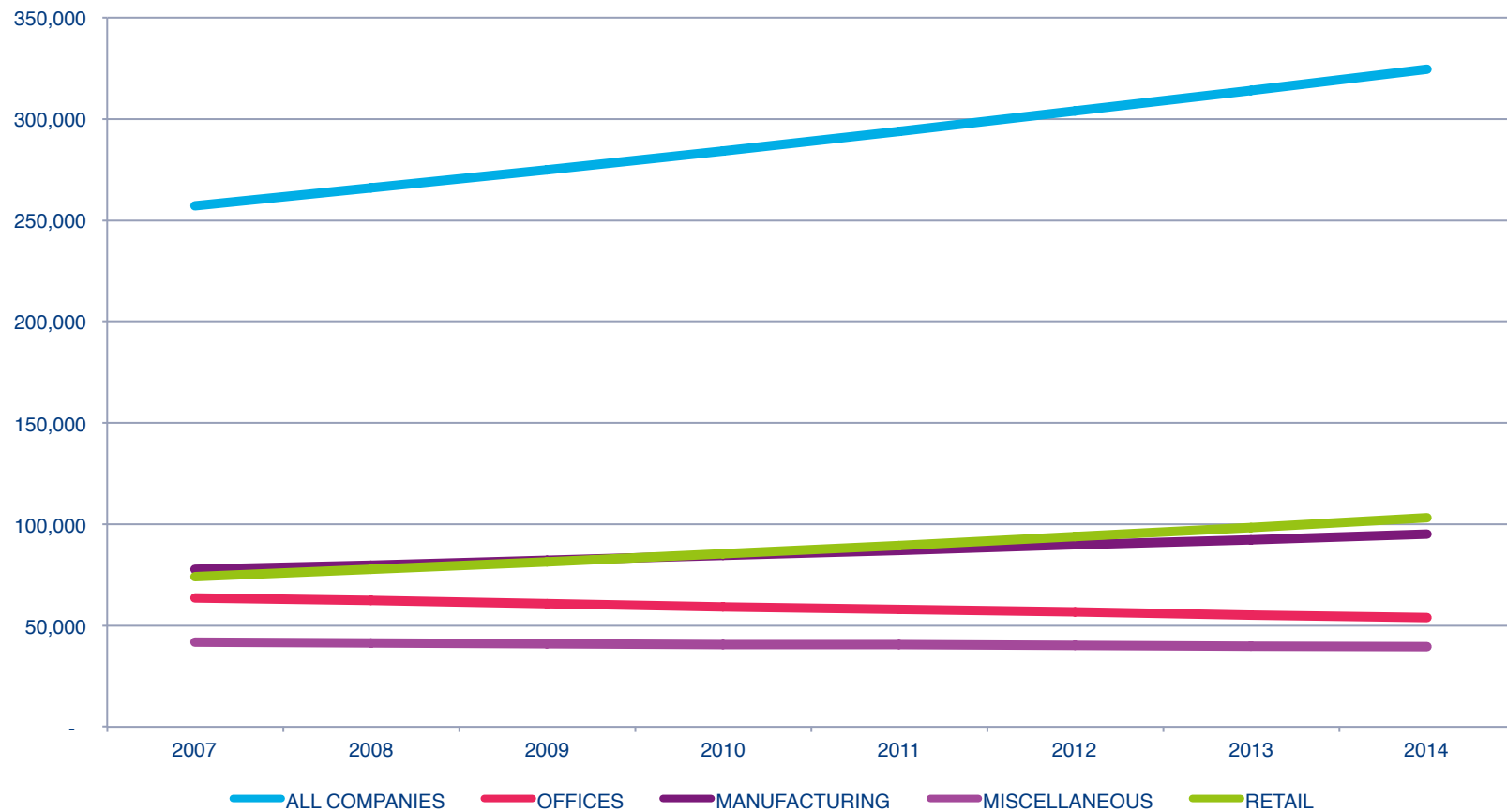
## H1: PREDICTED VALUES OF LEASES OVER 5 YEARS WILL FALL

### LEASE TERM OVER 5 YEARS



## H1: TOTAL CRE COMMITMENT WILL FALL

### TOTAL CRE COST



## **H1: CRE DECLINES OVER TIME**

- Length of leases over 5 years increasing
- Ownership increasing, bar Offices and Miscellaneous
- Total costs of CRE increasing, bar Offices and Miscellaneous

Increase in ownership arguably providing a more flexible portfolio.

Increase in lease length is not providing more flexibility



## H2: CRE FALLS AS TURNOVER/PROFIT INCREASE/DECLINE

### Positive Coefficient Independent Variables

- Previous Year's Profit – All Companies; Offices; Manufacturing & Retail
- Profit – Miscellaneous & Retail
- Turnover – Offices & Manufacturing

### Negative Coefficient Independent Variables

- Previous Years Turnover – All Companies; Offices & Manufacturing
- Profit – Manufacturing

Hypothesis broadly proven

<b>RETAIL - TOTAL CRE COST v PROFIT &amp; TURNOVER &amp; PROFIT MARGIN and TOTAL CRE COST v FTE</b>	<b>Estimate (Unstandardized Beta)</b>	<b>t-value</b>	<b>p-value</b>	<b>R<sup>2</sup></b>	<b>Adju. R<sup>2</sup></b>	<b>Sig. F Change</b>
				0.996	0.996	0.038
(Constant)	104.666	1.308	0.193			
Previous Year Total CRE	0.892	57.656	0.0			
Profit	1.264	5.918	0.0			
Profit Margin	-2,744.11	-3.496	0.001			
Dummy2	241.589	2.126	0.035			
Previous Year Profit	0.459	2.093	0.038			

### H3: CRE FALLS/INCREASES WITH DECLINE/INCREASE IN FTE NUMBERS

- Absolute Change in CRE cost per FTE: Offices -9%, Miscellaneous -0.6%, All Companies +8%, Manufacturing +20%, Retail +16%
- Positive coefficient FTE numbers with Total CRE Costs for All Companies & Manufacturing. Negative for Previous Year FTE Numbers

### H3: CRE LEASE COSTS DECLINE OVER TIME RELATIVE TO FTE NUMBERS

- Positive for FTE – All Companies, Manufacturing & Retail
- Negative for Previous Years FTE – All Companies, Manufacturing & Retail

Business increases space as it takes on people

Business is not reducing lease costs needs relative to FTE numbers

RETAIL - LEASE TOTAL v FTE	Estimate (Unstandardized Beta)	t-value	p-value	R <sup>2</sup>	Adju. R <sup>2</sup>	Sig. F Change
				0.992	0.992	0.013
(Constant)	-1.159	-0.038	0.970			
Previous Year Lease Total	0.958	65.691	0.0			
FTE	0.054	8.176	0.0			
Previous Year FTE	-0.051	-7.345	0.0			
Dummy7	-172.074	-2.523	0.013			

## CONCLUSION

- Evidence of improved portfolio flexibility and capability for *Dynamic Alignment* is limited
  - Only evident through increase in ownership
  - Lease increases reducing flexibility
- Relationships between variables not straight forward
- More consistency appears to exist across Manufacturing & Retail
- Further Work:
  - More granular analysis – business sectors, but sample size issue
  - Bring in other independent variables

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