The role of corporate real estate in developing countries of the Asia-Pacific region

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Abstract

This paper discusses the current role, multifaceted challenges and opportunities that the future holds for the corporate real estate (CRE) function and CRE professionals operating in developing countries, which often share several common trends. It identifies the drivers of change, as the real estate activity moves from a largely unorganised sector to an organised sector. It highlights the multifaceted challenges faced by the CRE function, eg talent acquisition and retention, 'work from anywhere' workplaces, centralisation of processes and the need for increased collaboration with procurement, HR, Finance and IT, etc. Finally

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it highlights how the CRE role is moving up the value curve and how CRE professionals are acquiring the skills and mindset of a 'solution provider' rather than merely a 'service provider'.

Keywords: organised sector, professional approach, solution provider mindset, workplace collaboration, the value curve, 'supporting' to 'owning'

INTRODUCTION

It is no surprise that, after the agriculture sector, it is the real estate sector that drives the highest level of employment in most developing countries; however, most real estate activity in these countries still lies in the broad category of an 'unorganised sector'. This is because a large number of the investments made in the housing sector are catered for by a large number of local and small developers/contractors. Therefore, compared to other industries in the organised sector, there has been much less deployment of qualified professionals or corporate practices in the real estate sector. But this trend is now changing, especially in the last two decades, due to rapid economic development in most of these developing countries. As a result, corporate real estate (CRE), as a discipline, is rapidly growing and continuously evolving to provide a professional approach to meet the real estate needs of multinational corporations (MNCs) operating in this environment.

REAL ESTATE AS A SIGNIFICANT CONTRIBUTOR TO APAC'S DEVELOPING WORLD ECONOMY

The contribution of real estate to the GDPs of many developing countries has been rapidly growing in the last decade, depending upon the state of the economy of these countries, with significant employment opportunities tied to their GDP share. For example, the GDP share of real estate in India was 6.3 per cent in 2013 and expected to generate 7.6 million jobs a year.[1] In China, the GDP share of real estate grew from 5 per cent in 2000 to 15 per cent in 2012, with 14 per cent of urban employment coming from real estate and related sectors.[2]

GROWTH OF THE 'ORGANISED SECTOR'

There has been a trend in real estate to move from an unorganised status to an organised one. The drivers of this shift are:

- accelerating growth of business process outsourcing (BPO) from this region leading to the entry of MNCs with specific and stringent real estate needs;
- rise of 'local-global' conglomerates as local businesses achieve global scales riding on huge domestic demand, as well as off-shoring of manufacturing, resulting in additional space and related infrastructure requirements like modern warehouses; and
- entry of large and professional business houses and private equity funds into real estate development/investment to cater for the underlying need for reliability of delivery, conformance to quality standards and sustainability, investment friendly business practices and the need for investment liquidity.

One indicator has been the growth of international property consultants (IPCs) in these countries, with most of the IPCs reporting a phenomenal rise in the number of their employees deployed in all aspects of real estate consultancy, ie transactions, facilities management, project management and, lately, portfolio planning and management. In addition, a large number of corporations that are occupiers of real estate now have real estate professionals within their organisation, either in-house or out-sourced, to add value to their real estate services for business stakeholders (Figure 1). Although the level of engagement within these organisations may be varied across different types of industry, it

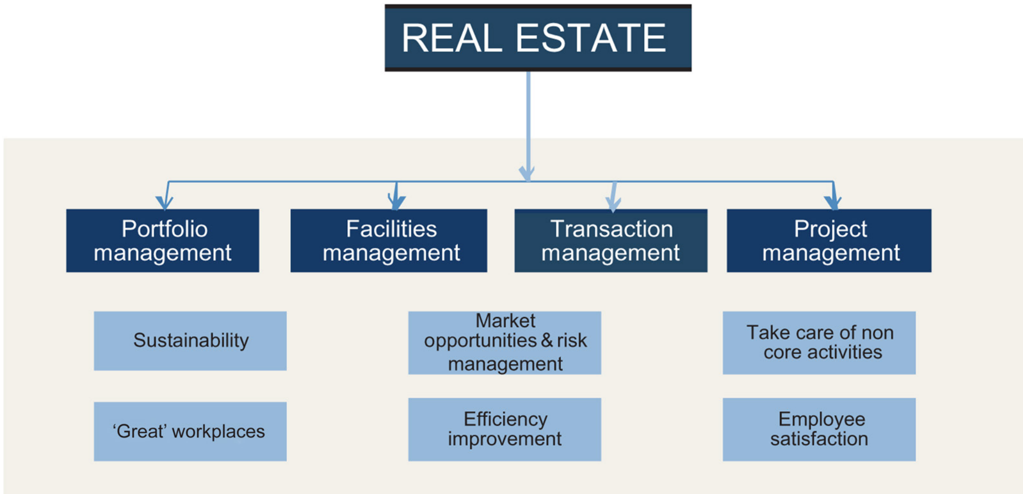

Figure 1 CRE value proposition
Source: Cushman & Wakefield

is growing rapidly, especially due to an awareness created by regular success stories in the press and educational efforts by several professional bodies like CoreNet Global, which is a leading association for CRE and workplace professionals and service providers.

Another interesting trend in the last decade relates to the growth of IPCs and other property consultants. Although initially these consultants were engaged primarily for real estate transactions, they made forays into facilities and project management that are now growing faster and form the bulk of their employee strength. This trend is expected to continue as real estate continues to move into the 'organised' sector and corporations wish to remain focused on their core business areas. Driving efficiencies in non-core areas like project execution and maintenance of facilities increasingly is being achieved through appropriate outsourcing. What is even more interesting is that, even in the housing sector that forms the bulk of the 'unorganised sector', IPCs increasingly are being engaged for sales transactions, project execution and even facilities maintenance, as house buyers become more discerning and demanding regarding reliability and quality.

CRE CHALLENGES

As CRE work matures in the Asia-Pacific (APAC) region, it is important to recognise some of the unique situations and challenges facing CRE professionals.

Attracting and retaining talent

Exponential growth in this region has created a dearth of qualified and experienced real estate professionals. Countries like India and China face the brunt of this talent war particularly regarding mid and senior-level management positions.

Governance processes

Most developing markets in the APAC region have limited access to information in the public domain. For most CRE professionals, combining governance needs with pragmatic delivery solutions can be a challenge. These challenges range from ensuring proper documentation for occupation to having to deal with differing legal opinions on titles, liaising with local statutory authorities and government bodies, dealing with complicated tax structures as well as possible involvement of labour or farmers in a dialogue on infrastructure or land deals.

Speed of delivery of projects

The cycle times for project delivery quite often are unpredictable. Projects have been known to take as long as 3–5 years to deliver, and there is the risk of a higher rate of failure in these markets due to litigation and changing policies. Clear planning, delineation of roles and responsibilities, monitoring and communication combined with strong relationship management with both internal and external stakeholders can be deciding factors between success and heartache. Therefore, in this region, for large transactions or projects, it is highly advisable to have early engagement of professionals from all levels of real estate services and to ensure adequate time for proper due diligence — often three months to a year to prevent any surprises.

Portfolio composition

In the APAC region, portfolios tend to be far more diverse both in terms of physical and geographic distribution as well as having to deal with multiple owners for a single site. For example, most manufacturing companies will have distribution sites that are owned or leased assets as well as third party service provider partnerships. Therefore, a single asset class of warehouses/distribution centres can have up to three distinct ownership models. For effective and efficient portfolio management and relationship building, one has to be aware of these differences. In addition, the growth of many corporations often has been in unrelated sectors, depending upon where opportunities were presented by the exponentially growing economies. For example, a company involved in the manufacture of salt may also run telecommunications services as well as being an airline provider. Also, as the growth of these companies is often through multiple acquisitions and mergers, they end up with a wide diversity of assets, which can range from traditional to speciality assets like tea estates, agriculture farms and employee housing. Therefore, the real estate strategic and planning inputs for their portfolio need to encompass a wide spectrum of asset classes and variety of applications. The added dimension of diversity in asset classes often makes it more challenging to add value by way of finding synergies in use, weeding out space inefficiencies and finally 'monetisation' of underutilised assets to support the overall business needs and future growth.

Consolidation of suppliers

Large organisations increasingly are centralising their support functions to drive professional and operational excellence, as well as to gain financial benefits from economies of scale. In recent years several initiatives have been seen, such as the 'power of one' initiative, which capitalises on a small, but highly focused and organisationally aligned, number of vendors for services, working as valuable partners. For example, at Unilever, the number of vendors for some services has been reduced dramatically from the earlier numbers that ranged in the hundreds across the regions. This reduction has been facilitated by centralised procurement functions with specialised skills for negotiating global 'master agreements', supported by local 'service agreements' in various geographies. Therefore, the CRE function also gets to share the aimed benefits although it requires a change in the ways of working and a far greater partnership with procurement. These changes are quite significant and their implementation often can be challenging for professionals in developing countries as, for historic and statutory reasons, their organisational structures tend to be autonomous.

Changing workplace processes

With the changing definition of what is a workplace (see Figure 2), CRE professionals now need to collaborate more extensively with internal stakeholders, including finance, procurement, human resources (HR) and information technology (IT), to sense the pulse of employees and their changing expec-

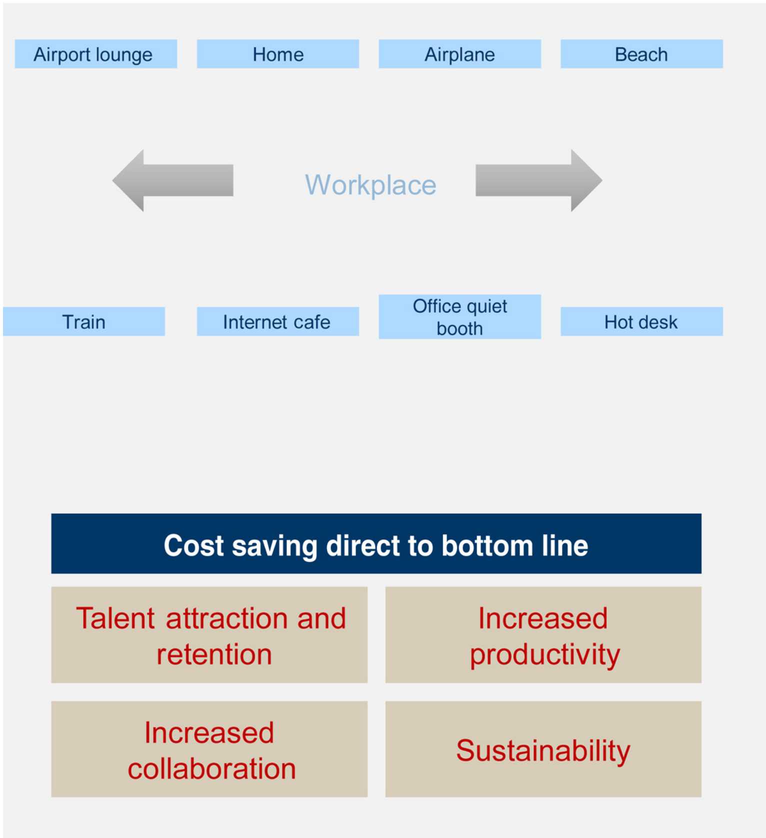

Figure 2 Work is no longer a place you go to
Source: Cushman & Wakefield

tations of work spaces and technology, and to ensure that the shelf life of their real estate choices is reasonably long. To rightly earn their seat at the decision-making table with senior leaders, CRE professionals need to increase their financial acumen and acquire other functional skills in order to provide a comprehensive business case, which not only covers real estate considerations, but also encompasses other business-related parameters. This only can be achieved by dovetailing real estate strategy into business strategy with the help of finance and business partners. Sustainability is very high on the agenda of most organisations. For example, the Unilever Sustainable Living Plan has set the goal of halving the environmental footprint in the making and use of their products by 2020. This includes specific and ambitious workplace targets to reduce energy, water and waste. Similarly, many other organisations have set clearly defined targets for reducing energy and water consumption, which consequently greatly impact the choices they make in their real estate decisions, throughout the life cycle of the property.

Benchmarking and research

Senior business stakeholders now demand more data-based decisions and, consequently, CRE professionals are increasingly required to share with them key market practices, risks and opportunities in advance, when recommending any real estate solutions. Decision making has moved towards being more objective and process-oriented rather than just being based on business relationships, emotions and 'gut feel'. This decision making requires an incisive analysis of market trends backed by reliable and continuously updated data from a wide variety of sources, as well as suitable research to enable scenario building and good forecasting. IPCs, therefore, have stepped in to fill this important need by having dedicated market research teams for the benefit of their clients, and they issue regular reports for all geographies.

CRE ORGANISATION: EVOLUTION FROM 'SERVICE PROVIDER' TO 'SOLUTION PROVIDER'

In view of the challenges explained above, the CRE function has been changing gear to provide timely and 'fit for purpose' solutions that enhance business performance. Over the past 15 years, CRE has evolved in the APAC region from *ad hoc* use of local brokerage by various functions within the organisation to a sophisticated model charged with client relationship management (CRM), governance and cost optimisation. The mindset is fast changing from that of a reactive internal 'service provider' and 'order taker', having to meet a lower level of performance metrics, to that of a proactive 'solution provider' often taking on audacious targets to support business goals (Figure 3).

Change has been primarily driven by MNCs seeking a consistent service platform across a region or globally, supported by professional property companies. Interestingly, the frequency of paradigm changes tends to follow the economic cycles. When markets are booming, and businesses are doing well, there is less attention on real estate efficiencies and decisions tend to be more reactive and driven by immediate growth needs. When there is a downturn in the market, the business focus shifts from rapid expansion to shoring up the bottom line through aggressive cost-savings. Given that real estate typically tends to be among the 'top five' cost centres in an organisation, effectively managing a real estate portfolio will result in a direct impact to a company's financial objective. Therefore, business stakeholders are more willing to consider changes and new ideas from CRE teams during this period. Typically, IT and telecommunications (IT&T) companies have been ahead of the curve when it comes to building

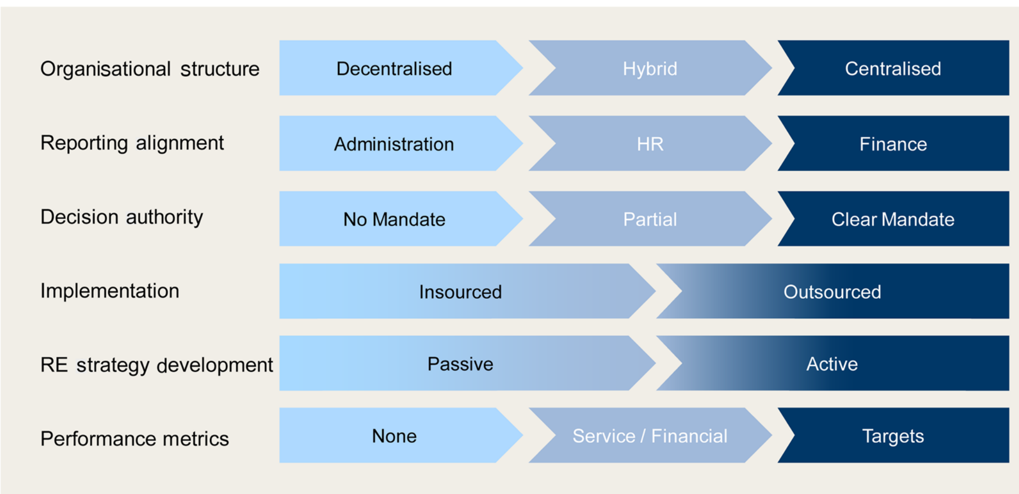

Figure 3 Possible organisational structures and their implications
Source: Cushman & Wakefield

CRE teams and partnering with property firms for delivery, while more traditional sectors, such as manufacturing, have been late starters, although there are some notable exceptions (like Siemens), with some embarking on the journey 18–24 months ago.

The evolution of outsourcing real estate services in the APAC region has been driven mainly by US companies, which tend to be more centralised with CRE teams having direct reporting into the USA. European companies are generally seen to operate in a far more decentralised fashion, allowing local business units far greater autonomy in decision making. In more mature markets, the focus is on building relationships with the business and other internal stakeholders, taking on a larger CRM role, but it is critical to note that, in less-mature markets, it is incumbent on CRE professionals to build strong relationships with external stakeholders such as developers and landlords, as well as to gain the support of the legal and other tertiary professionals who ensure the smooth delivery of projects.

Reactive to proactive

The goal of the CRE function is not just being able to respond to an immediate business need, but to actively engage with the business on a continuous basis and bring opportunities for them to consider as well as plan around risk mitigation of the portfolio. The last 3–4 years have seen the emergence of strong account management teams by service providers in the region, in anticipation of proactive portfolio optimisation by occupiers, and today there are many CRE teams planning strategies 2–3 years in advance of expiry events, taking advantage of market and lease situations where possible, and constantly reviewing the portfolio.

THE FUTURE: THE VALUE CURVE

The real estate industry has seen a shift in the operating models, varying from *ad hoc* to a single source; however, the tide seems to be turning now from pure 'best cost' decisions to a more integrated 'value proposition' approach. Greater global accountability, following the Enron and WorldCom meltdowns, has increased the level of corporate governance, and this is now a key element of consideration which has driven many corporations to review how their real estate is being managed. While US companies have tended to be more centralised and manage their real estate globally, the checks and balances have been increased. For European companies, it has meant greater centralisation of the real estate function within the region, and restructuring traditional CRE teams to better serve companies' changing needs. A centralised function also benefits the corporation in allowing for a holistic view of its portfolio, supporting questions of which locations offer the best talent and incentives for their business. Occupiers are also recognising that very different skill sets are required to visualise and drive 'planning and strategy' for real estate as compared to delivery and operational issues, and there is a shift to separate these roles to ensure maximum expertise in both spheres. It is no longer about a single transaction, but actively seeking not only to deliver greater value to the business, but also to bring ideas and innovation to the table.

The two ends of the spectrum on the value curve for CRE have been the IT&T sector at one end of the scale and the manufacturing sector at the other end (Figure 4).

Telecommunications and technology

IT&T has been the pack leader with most companies having a centralised CRE function globally and regionally. The focus of these real estate teams is on speed to market, adapting to technological changes that affect its business model and further optimisation of its portfolio. Workplaces for these firms tend to play a big part in the key considerations of employee attraction and retention.

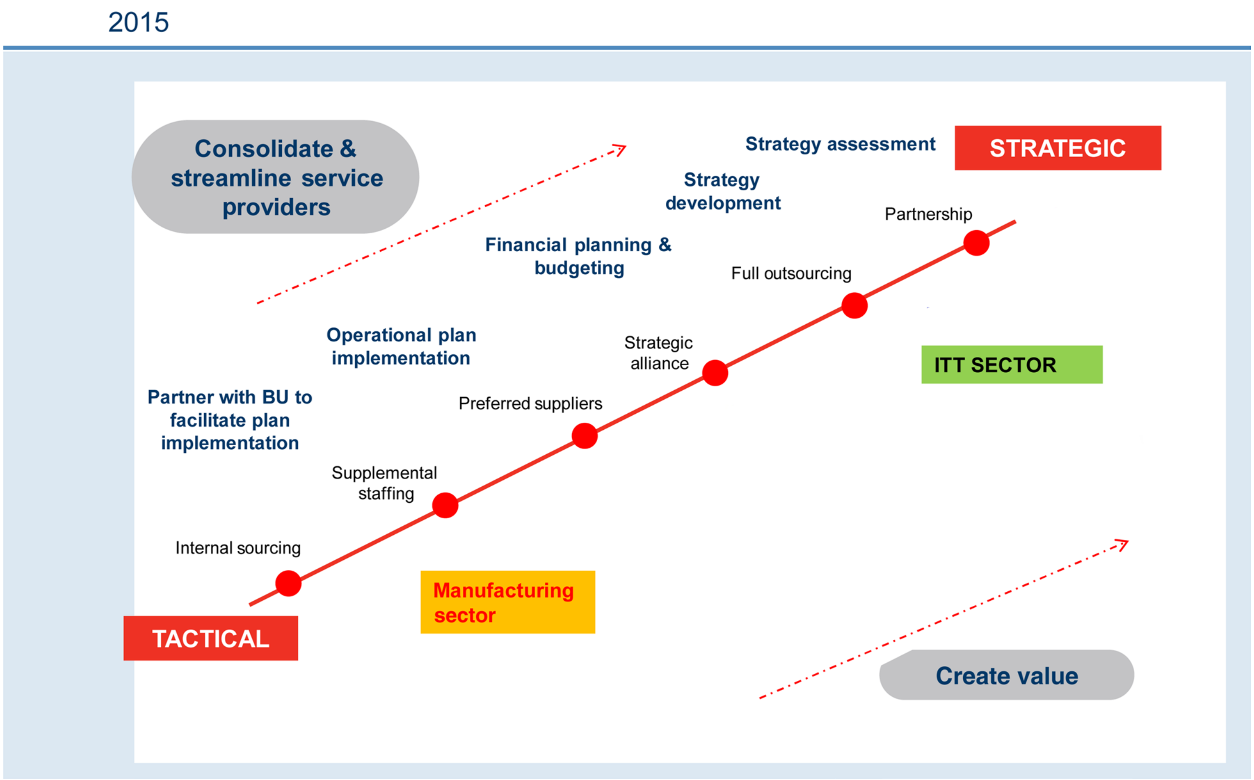

Figure 4 Where corporations are positioned today
Source: Cushman & Wakefield

Manufacturing/fast-moving consumer goods/pharmaceuticals

This sector has been a relatively late entrant to the world of outsourcing, with some exceptions, and several well-known household brands have started their journey and are continuously improving their models to suit their companies' objectives. The trend of outsourcing follows the change in the CRE organisation and can range from a single-source supplier to a hybrid of panel suppliers to ensure best-in-class local service delivery. A key challenge is educating the business on the benefits of moving to a centralised system from a decentralised one. Many of these companies have been in these countries for decades and often operate like a local firm. Very often they have been the pioneers in these markets and local operations have dealt directly with real estate matters themselves.

CONCLUSION

The purpose of this paper has been to highlight the evolution, challenges and ways in which the CRE function as well as the professionals within that function are moving up the value chain to influence and guide decisions objectively. At the top end of the spectrum there have been efforts made by some companies whereby the real estate function operates with profit and loss (P&L) accountability, truly accounting for the optimum use of every square foot of real estate held by the company. Siemens is one of the few companies to have carved out Siemens Real Estate as a separate P&L account centre. There are other companies, like Unilever, GE and Pfizer, which have strived to move up the value curve by bringing their global real estate assets under a single control function supporting the business. This move has provided a key opportunity to step-change the management of their portfolios, shifting from supporting to owning and driving ambition with a clearly defined vision to provide best-in-class management of real estate. Clearly there is no 'one size fits all' strategy for managing the real estate portfolio and various organisations continue to choose the models that best suit their organisational goals, within the context of the size of their portfolio and geographical location.

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