

CORPORATE REAL ESTATE FUNCTION: A REVIEW

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ABSTRACT

Nowadays, the indicators used to determine the real estate's contribution to business activities in most organization are primarily focused on cost reduction or capital minimization. However, what is often not realized is that property can also assist revenue enhancement. This paper highlights the synthesis of previous studies from 1990 to 2010 in relation to the corporate real estate function. The considerations include the task of CRE executives that influence the shareholder's wealth. The trends of the corporate real estate function are discussed. In summary, by recognizing the important of CRE function, it will provide the greatest support to CRE executives in public listed companies to enhance share price performance and dividend growth.

Keywords: Corporate Real Estate, CRE's function, shareholder's wealth

1. Introduction

Corporate real estate (CRE) comprises land and buildings owned or leased by companies not primarily in the real estate business. It becomes a part of the overall investment portfolio that the management must deal with in order to maximize shareholders' wealth. Maximizing shareholder wealth is the single most important goal for any profit seeking organization and as such it becomes extremely crucial for them to achieve higher profit.

Nowadays, CRE executives are challenged with articulating how real estate can have a positive financial impact and contribute measureable value to the organization. For many companies, real estate is not adding shareholder value and it is perceived to be 'an operational pain' for them.

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Therefore, they classify property as a cost of doing business rather than a value adding opportunity. In 2006, research by Lindholm, *et.al* found that many firms still do not recognize the strategic potential of their real estate especially on how real estate adds value to the business.

On the other hand, Currie and Scott (1991) found that real estate represents on average 150 percent of net assets, a substantial proportion 30-40% of total assets, and 100 per cent of capital in the balance sheet of industrial companies. Real estate becomes part and parcel of the companies as they grow, intertwined with the business operation (Hiang, 1999). Bannock & Partners (1994) revealed that among large UK companies, property represented 16-20% of total costs. Real estate has a very direct impact upon shareholder value and for companies looking to increase value, controlling the cost base is the quickest and most direct solution (Booth, 1999). From an international perspective, the ownership of significant amounts of real estate by corporations in the US is well documented, estimated approximately at about 25% of corporate wealth (Rodriguez & Sirmans, 1996). Surprisingly, more than 25 per cent of corporate assets consist of real estate, and occupancy and property costs become the company's second-largest expense item after wages and human resources. The CRE function is generally not considered as a strategic field of corporate management within the organization (Rodriguez and Sirmans, 1996).

In recent studies by Arthur Andersen (1993) and IDRC (Lambert *et al.*,1995), they validated that many CRE executives still protest that their senior management will not provide them with sufficient influence to reach the greater impact they believe real estate strategy and decision making can have upon the wealth of their company's shareholders. Manning and Roulac (1996) research indicates that senior management has looked to their CRE function primarily to improve operational efficiency and reduce costs and has not sought CRE assistance with strategic planning, either at the corporate or business-unit levels.

This paper presents a synthesis of some studies from 1990 to 2010 on corporate real estate function. The aim of this paper is to recognize the trend of studies concerning the task of each level of CRE and the power of CRE executives' skills in order to maximize shareholder wealth.

2. Trend of Studies in CRE Function

Previous studies on corporate real estate function have been undertaken in various settings: manage CRE much more professionally and creatively; Joroff (1992), McLean III (1993), Nourse and Roulac (1993), Arthur Andersen (1993), Lambert *et al.* (1995), Cameron and Duckworth (1995), describe function by each levels of CRE; Manning and Roulac (1996), Manning, Rodriguez, Roulac (1997), Organization, authority and influence O'Mara *et al.* (2002), and focus on maximising shareholder value; Hill (2001), Wills (2002), Lindholm and Levainen (2006), Trundle (2005), and Liow and Nappi Choulet (2008). It was obvious that the trend and research concern of previous studies have changed over time (Figure 1).

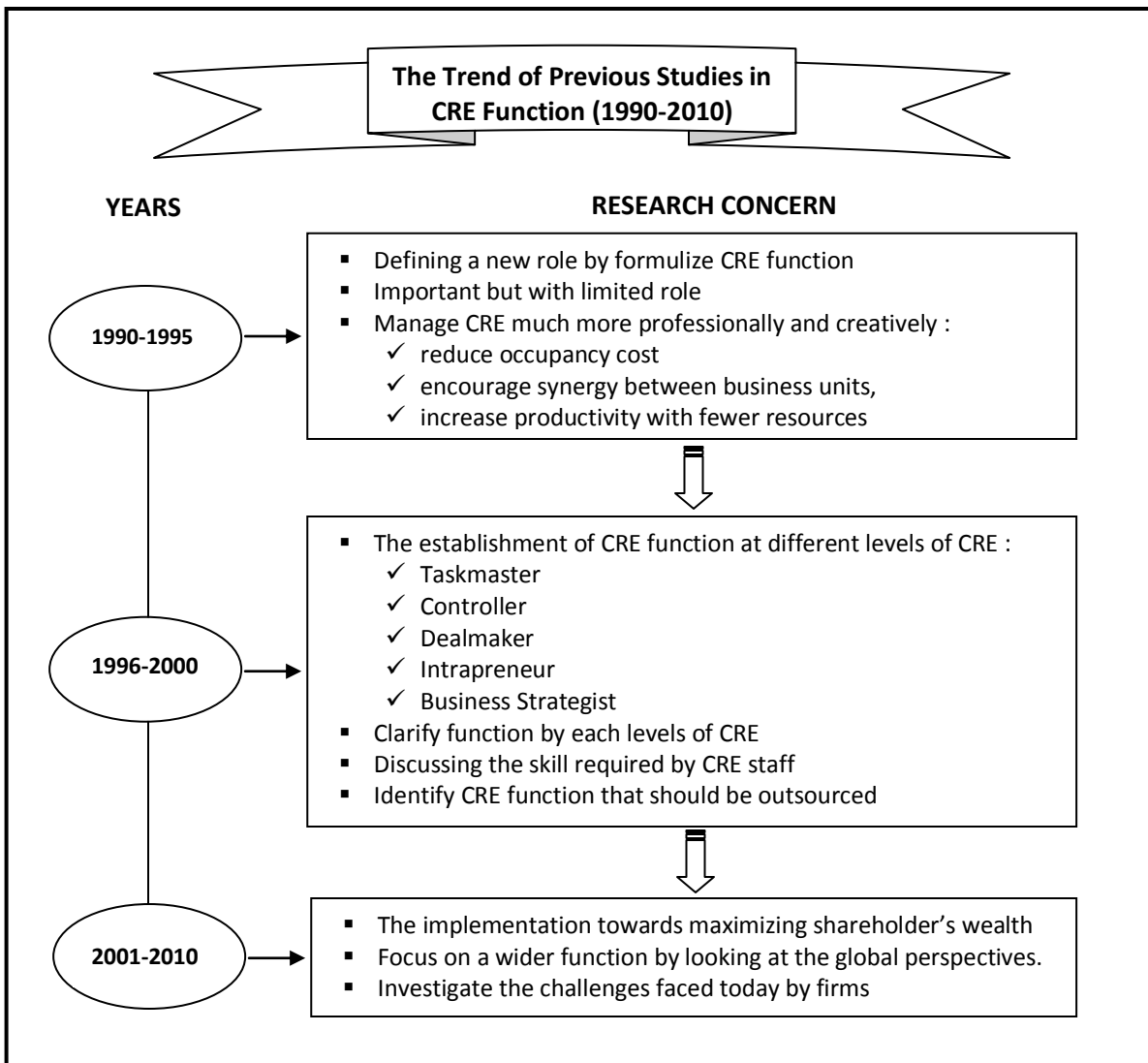


Figure 1: Trend of Previous Studies in Corporate Real Estate Function

2.1 Phase 1 (1990-1995)

Figure 1 describes the trend of previous studies in CRE function from 1990 to 2010. This table categorize this studies into district phases. In the early phase (1990-1995), the contribution of corporate real estate function was important but with a limited role. For example, based on research by Arthur Andersen in 1993, it was found that senior management was reluctant to believe that the CRE function provided an opportunity to impact shareholder wealth. On the other hand, CRE executives always believed that efforts and alternatives from their department in reducing their company's occupancy cost and improve operational efficiency provided major opportunities to impact shareholder wealth. However, these findings contrasted with Joroff *et al.* (1993) when they stated that senior managers were now starting to realize that real estate is a critical strategic asset, one that supports the financial, work environment and operational needs of the total corporation. Besides that, in this phase, CRE executives were responsible to manage CRE much more professionally and creatively such as reduce occupancy cost, encourage synergy between business units, and increase productivity with fewer resources. McLean III (1993) asserted that Hewlett Packard (HP) had taken a proactive and strategic approach to their real estate portfolio management; one of their alternatives in an all-out campaign to reduce occupancy costs. Besides, the research concerned with this early phase emphasized defining a new role to formalize the corporate real estate function and many studies highlighted the development of strategic planning for the entire real estate portfolio.

2.2 Phase II (1996-2000)

The second phase (1996-2000) followed by describing the function by each level of corporate real estate. Actually, prior to this period, it had been difficult to define the CRE function terms because there were no specific answers for this question. However in 1996, Manning and Roulac organized the CRE function in a structured way by classifying it according to the levels of corporate real estate. Discussion in the literature of Manning and Roulac (1996) on structuring the corporate real property function for greater "bottom line" impact emphasized the role played by CRE staff in order to contribute more to shareholder wealth. They described the CRE function based on each level of CRE staff. Actually, this function had been discussed before in Joroff

(1992), followed by Lambert *et al.* (1995) and Cameron and Duckworth (1995). All of them agreed that each higher level capacity would have increasingly greater impact upon shareholder wealth. Each higher level necessarily builds on the skills and knowledge acquired in the prior levels. All different levels of the CRE function are summarized and shown in Table 1.

In Joroff *et al.* (1993), they discussed the evolution of real estate mission. Early in the 1980s, CRE units expanded their function from a technical Taskmaster who just maintained the operation of building's to Intrapreneurs who generate profits through real estate development. While in the 1990s, this evolved to the Business Strategist which addressed overall company competitiveness. This evolution supports the continuous improvement in the CRE function.

Manning and Roulac (1996) suggested that additional research in this area had the potential for providing the greatest support to corporate real estate executives to explore, enlarge and customize their tasks for better impact on their company's strategic planning and shareholder wealth.

Table 1: Corporate Real Estate Function

LEVEL OF CORPORATE REAL ESTATE	FUNCTION
Taskmaster	Procure cost-efficient facilities
Controller	Standardize space needs to minimize facility occupancy costs
Dealmaker	Creative space-needs, problem solving and negotiation re specific assets
Intrapreneur	Provide real estate services as a competitive service provider
Business Strategist	Integrate workforce, workplace and technology trends into overall business strategy

Source: Manning and Roulac (1996)

The following provides a more detailed discussion of the five levels of CRE function explained in the order of their enhancing opportunity to impact shareholder wealth :

1. Taskmaster

Taskmasters emphasize the engineering approach and procure cost-efficient facilities by working with business units. The primary goal is to provide facilities that support normal business activities. The involvement of senior management at this level was generally limited to periodic reviews of corporate real estate performance. This level requires strong technical abilities.

2. Controller

The aim of this level is minimizing total facility occupancy cost. This stage not only emphasizes cost-effectiveness, but it also focuses on generating benefits from real estate assets. For example, manage their space efficiently at the lowest possible cost and the use of basic inventory and cost-control methods used throughout the corporation. In order to achieve their aim, they need to standardize employee and operating space needs by cooperating with upper levels of management with senior management more directive at this levels. As a controller, CRE executives should have greater analytic skills especially in accounting. Even though in Level 2, controllers are responsible for standardizing employee and operating space needs, it doesn't mean that they are able to make a decision on a work space without discussing with their senior management first.

3. Dealmaker

Dealmakers focus on applying standardized project-related negotiation and problem solving abilities to a business segment's changing space requirements. Undeniably real estate most closely aligns with the finance department. Apart from that, dealmakers creatively negotiate on behalf of the overall company to seize opportunities to save money through financial, organizational and site selection associated with individual company assets by structuring innovative projects to lower costs and generate income. Besides having a strong project-related negotiation ability and imaginative problem-solving skills, the most important skills that this level should have is effective communications with other units. According to Lambert *et al.*'s (1995) survey, they found that the most services provided by CRE executives is on Level 3 Dealmaker project-oriented activities. While, Manning and Roulac (1996) supported this finding by mentioning that these standardized activities are consistent with the emphasis on cost-cutting in corporations.

4. Intrapreneur

Intrapreneurs working with business-unit executives is a competitive real estate operation in its own right, "benchmarking" their performance in terms of both cost and quality of the real estate services and products they provide. In simpler words, business segments become real estate customers. Consequently, working with business-unit managers, as well as people from human

resources, information services, sales, and marketing, CRE managers discover production innovations, enhance productivity and participate in the business unit's strategic planning process through the provision of needed occupancy cost data. In addition, the concentration shifts from the building and facilities to the portfolio and involve both the unit's and the corporation's mission and planning processes (Joroff *et al.*, 1993). This level requires technical and people skills, besides the need to fulfill the requirement of management and financial expertise. As an Intrapreneur, working with business-unit managers with cost-information requires CRE staff to learn the business of the business-unit managers while demonstrating quality cost-effective real estate services (Manning and Roulac, 1996). Lambert *et al.* (1995) advised that CRE units must understand and develop the knowledge of asset management in Level 4 Intrapreneur first before moving forward to the next step (level 5 Business Strategist) to fulfill their mission. One of the Intrapreneur's important role is "benchmarking" their success with business units and reporting their success back to both business-unit decision makers and senior management. The reason behind it is because this effort can convince and prove to managers the value of including expanded customized real estate input to their operating and strategic decision making processes.

5. Business Strategist

At this level, real estate executives accept and implement the opinion of senior executives. Business Strategists are working with senior corporate and business unit managers to integrate workplace, workforce, and technological trends into a broader strategy that will enhance competitive advantage, productivity and shareholder value. CRE staff work with "stakeholders" within the company, combined with outside resources and service providers, to anticipate business trends, monitor and measure their impacts, and contribute to the direction of the corporation as a whole through the development of an occupancy strategy. This level requires a global outlook of the corporation's initiatives, a mind-set that encourages a new transformation as the agent of progress, and the ability to promote innovation in the work of line managers. Manning and Roulac (1996) observed that among all levels of Corporate Real Estate discussed, Business Strategists play important roles in developing competitive advantage, productivity and shareholder value. They also mentioned that the Intrapreneur and Business Strategist tasks of the CRE staff have the potential of contributing hugely to shareholder wealth due to the unique

integrative way these positions involve virtually all staff functions (e.g., accounting, operations, marketing, MIS, human resources, etc.) as well as the operating business units of a big company. This opinion was supported by Lambert *et al.* (1995) who viewed the understanding of Intrapreneur and Business Strategist about the corporate culture as well as the requirements of business unit and they can be trained to manage real estate. However, before contributing significantly as a Business Strategist at the business-unit level, CRE executives must first win over business-unit managers with their transactional real estate support (i.e., at the Taskmaster, Controller and Dealmaker levels) and truly observe the businesses of the business units they provide.

However, outsourcing the CRE function was also a research concern during this phase. The function associated with the first three levels of CRE could be outsourced, but the higher levels would be carried out more effectively by internal managers (Manning, Rodriguez, Roulac (1997).

2.3 Phase III (2000-2010)

In third phase (2000-2010), studies focused on a wider function by looking at the global perspectives. For an example, O'Martha (2002) described CRE function in three spectrums, namely organization, authority and influence. At this phase, studies investigated challenges that firms are facing today. However, the trend of studies in CRE function are focusing more on maximizing shareholder wealth, Hill (2001), Wills (2002), Lindholm and Levainen (2006), Trundle (2005), and Liow and Nappi Choulet (2008). In making any business decisions, shareholder wealth maximization should be seen as the ultimate goal. This fact is agreed by the extent of theoretical and empirical research in finance economics as observed in Krishnan (2009).

Actually, many companies still do not understand what the thinking behind shareholder value is. Therefore, it is no wonder that they classify real estate as a burden or an 'operational pain' which is unable to contribute on shareholder value. However, Hill (2001) had emphasized how corporate occupiers can manage the contribution that their operational properties make to

shareholder value. According to Wills (2002), the most important thing to be considered is it possible to measure the wealth effects that CREOs are creating by looking at the establish role of the corporate real estate manager/team in their corporate framework.

It is well known that occupancy costs become the largest proportion of most fixed costs. Therefore it plays a very significant responsible for CREO in driving shareholder wealth. In a well-organized capital market, the cost is only related to the risk that investors cannot remove by holding a basket of shares even if a firms pay investors for the use of capital. Besides that, cost management becomes a main focus for CRE executives in providing their services. Bouris (2005) declared that there is one approach to express the contribution of CRE value which is by identifying the links between real estate activities and specific financial statement drivers.

3. Discussion

It was obvious that the trend and research concern of previous studies have changed over time. In the early phase (1990-1995), the contribution of corporate real estate function was important but with a limited role. The research concerns during this early phase emphasized defining a new role to formalize the corporate real estate function. While, at the second phase (1996-2000), studies emphasized tasks of CRE function based on each level of CRE staff. Actually, this function had been discussed before in Joroff (1992), followed by Lambert *et al.* (1995) and Cameron and Duckworth (1995). However, in 1996, Manning & Roulac have emphasized their studies on the role played by CRE staff in order to contribute more to shareholder wealth. In the management of finance's context, each level of CRE function plays an important role to achieve their goal in maximizing shareholders' wealth. Starting from the Taskmaster level, it takes an engineering approach. Joroff *et al.* (1993) mentioned that the actual real estate costs are not imposed on occupants since facility costs are often treated as overhead. For that reason, they are not part of facility requests or provisions. Then, it is followed by the Controller who seeks to minimize cost. The next level is the Dealmaker, a role which is associated with market cost and usage strategy, while the Intrapreneur is concerned with market design strategy. However, the Business Strategist has it's own and unique role in the management of finance's context. The demands of the corporate capital structure are fully combined with the needs of business unit.

Costs reflect real estate and corporate capital market costs. At this level, business units are required to validate the actual costs of occupancy. All in all, the best approach for each level depends on the individual corporation's needs. Some may prefer the less market-driven approaches while others run two of the levels at one. In the third phase (2000-2010), studies stress a broader perspective on the CRE function with the emphasize on challenges that firms are facing today. Most of the studies in CRE function at this phase focus on how to fulfill the corporate goal and maximizing shareholders' wealth. However, CRE needs to be well organized in a rigorous and structured manner before the corporate can consider achieving their targets. If a company wants to refresh their company's financial health, they should take into account the participation of CREO in a management team. This alternative will give a CREOs opportunity for them to respond to new and developing needs of company.

4. Conclusion

This study on the history of CRE research has been undertaken to provide a greater understanding of the CRE function. CRE function will give a greater impact on company's shareholder wealth if the CRE executives make the right financial decision in relation to their real estate assets. The most important thing to be considered is that the CRE function should be aligned more efficiently with corporate objectives. Apart from that, senior management should put more faith on the capability of CRE function which has a significant prospect to increase shareholder wealth. Further research is needed to develop a framework of corporate real estate function through integrating organisational strategy towards shareholders' wealth maximization. As the conclusion, the result of this research would serve as an important guidance to CRE professionals in understanding the CRE function, which may help them in leading CRE practice particularly when aligned, and ideally integrated with the organizational strategy.

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