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AUSTRALIAN CORPORATE REAL ESTATE MANAGEMENT: IDENTIFICATION OF THE HYBRIDISATION OF PROPERTY AND FINANCIAL KNOWLEDGE IN PRACTICE

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Abstract

The study of Australian Corporate Real Estate (CRE) management is an emergent field. As part of an enquiry into competitive practices in Australian CRE, focus groups were held to identify current and future Australian issues. One group's participants were drawn from corporate organisations, the other predominantly from local government. While each group emphasised different aspects of CRE management, a common listing of findings is possible. The hybridisation of property and financial knowledge in the practice of CRE management is evident in five aspects of the issues discussed – the need for the alignment of organisational and CRE strategies, the decision-making methods, the skill-sets of CRE managers and outsourced service providers, and the organisation of CRE management.

Keywords

Corporate real estate, strategic management, focus groups

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Introduction

Financial issues and the role of real estate as an investment have typically dominated research into property. In recent years, however, real estate has come to be seen as a facilitator of an organisation's operations. In line with this new role, increasing attention has been given to the management of real estate.

Described as Corporate Real Estate (CRE) management, this is the management of real estate by an organization which incidentally holds, owns, or leases real estate to support its corporate mission (Rondeau 1992:1; Bon et al. 1998:209; Brown et al.1993). The primary value to the organisation is not the investment value of the property but its contribution to the way it does business. Management techniques to derive operational benefits from the property include site selection, facility design, and space utilisation (Manning and Roulac 1999:268).

An awareness of the value of real estate in support of business operations dates from the early 1980s. Zeckhauser and Silverman (1983) identified that between 25% and 41% of corporate assets are real estate. Subsequent research (Veale 1989) showed that property occupancy costs make up 10-20% of operating expenses, or 41-50% of net operating income. Since the early 1980s much research has been carried out in Europe (predominantly the UK) and North America (predominantly the USA). The European studies include an ongoing comparative study of European and North American CRE practices and attitudes to CRE management (Bon 1996; Bon and Luck 1998; Bon and Luck 1999), management tools (Lopes 1996), a meta-model for CRE management (Lopes 1997), the value of CRE management (Krumm et al. 1998), changing office needs (Dent and White 1998) and flexibility in property suppliers meeting changing corporate requirements (Gibson and Lizieri 1999). In the USA, significant studies include

managing real estate to provide value (Apgar IV 1995), information technology (Johnson et al. 1997), benchmarking performance (Noha 1993), outsourcing (Bergsmann 1994; Manning and Roulac 1997). In a recent article, Manning and Roulac, (1999) document and summarise the status of CRE research, particularly that carried out in the USA.

The strategic implications of CRE were identified as early as 1986 (Roulac 1986; Roulac and Cameron 1987), but it was only from the beginning of 1990s that they gained recognition alongside other pragmatic management concerns (Joroff et al. 1993; Nourse and Roulac 1993; Duckworth 1992; Weatherhead 1997; O'Mara 1999). Because the strategic implications of CRE have only received significant attention in the last decade, it may be described as an emergent field of research.

Interest in CRE research has also increased in Australasia in recent years (Teoh 1993; Adendorff and Nkado 1996). In Australia, this interest has been driven by domestic demand for attention to be given to the needs of CRE in organisations.¹

This study explores current attitudes and beliefs about CRE management in Victorian based organisations. This research investigates the relevance of issues identified in international CRE research to the Australian context. Understanding attitudes of key property managers to financial and business management, as well as their more familiar property management domain, is an important step in understanding the role of the CRE unit in the organisation. To this end we used focus groups of CRE experts.

¹ Evidence of this is the Victorian Department of Infrastructure together with the Property Council of Australia (Victoria) and Australia Post providing funds supporting a collaborative research project funded by the Australian Research Council (ARC) exploring issues in Australian Corporate Real Estate.

The results indicate that CRE management spans two realms, the first being financial and business management², the second property management. Bringing these realms together is evident in five aspects that are identified and discussed. These may be summarised as:

1. Strategic alignment between CRE and the organisation as a whole;
2. Decision-making requires that business, or financial, and property decisions are established independently before being brought together;
3. CRE management bridges the business and property realms, requiring the skill-set of CRE managers to be a hybrid of both;
4. The skills required for the strategic management of real estate may not exist in the service provider market; and
5. A strong CRE management unit serves the organisation by spanning between financial and operational levels.

Aim

The overall aim of the research was to identify key issues in Australian Corporate Real Estate management using a focus group methodology. Issues in CRE management have recently been examined in a North American context (Carn et al. 1999) and we do likewise from an Australian perspective. Responses were sought in the areas of strategic management of property, financial methods, decision-making methods, CRE skills, outsourcing issues and performance evaluation methods.

This paper explores the current attitudes and practices of industry leaders in CRE management and gives indications of future directions. Particular emphasis is given to financial and strategic management in

comparison to property management, and the interaction between the two

Method

Focus groups were selected as the research method because they yield qualitative, contextual data appropriate to the examination of complex issues. The groups were a purposive sample drawn from CRE experts in Victorian based organisations. Participants were familiar with strategic CRE management and were from organisations with substantial property portfolios.

Corporate organisations have usually been the focus of research into CRE and therefore made up one of the focus groups (corporates sector). However, government organisations also hold significant property portfolios, and thus a second group was assembled from Local and State government organisations (government sector). Table 1 summarises the sampling outcomes with regard to organisational type and participant numbers.

Table 1

| Sector | Approached | Agreed to participate | Participated |
|----------------------------|------------|-----------------------|--------------|
| Corporates | 15 | 8 | 6 |
| Government (Local & State) | 16 | 7 | 4 |

While the recommended number of focus groups is between 3 and 5 (Morgan 1998: 77) and the recommended number of participants ranges between 6 and 12 (Morgan 1998:71), fewer groups are acceptable where there is a limited diversity of opinion and smaller groups are very suitable where the participants are experts in the topic being examined³ (Morgan 1998:77).

² In this paper the notions of financial and business aspects are used interchangeably as they represent similar aspects of a single body of knowledge.

³ The research program had previously ascertained that the pool of available CRE experts in the potential sample population was not extensive.

Prior to conducting the focus groups, a structured guide was prepared, which included trigger statements to prompt discussion. The trigger statements were organised in the following topic areas:

- Making CRE more strategic
- Organisation of CRE within the firm
- Performance measurement
- Financing CRE
- View of CRE within the firm
- CRE decision processes
- Skills needed by CRE managers in the future

During the sessions a further question was put to the groups examining

- Governance within the organisation and the relationship to CRE.

Data capture

The groups were recorded with 2 omnidirectional mikes recording onto a 2-track digital tape via a mixing deck. The digital recordings had their signal strength adjusted and background noise masked prior to being transferred to analogue audiocassettes.

Transcripts were prepared from the cassette tapes, checked to ensure fidelity of transcription and revisions made to match the transcripts with the audio recording.

Analysis

Based on guidelines recommended for focus groups (Krueger 1998) it was decided to analyse the focus groups' transcripts using qualitative analysis coding techniques. Qualitative research methods (Miles and Huberman 1994; Burns 1997) provided detailed methods for the analysis.

Initially a categorisation process was used to identify the transcripts' broad conceptual themes. The categories were developed from the trigger statement topic areas and the titles of groupings of similar practices from other research into CRE

practices. These categories were assigned master codes with sub-codes related to specific topics grouped under the master codes. The sub-codes were developed from the trigger statements and the practices from the research into CRE practices (Refer the Appendix for codes used and their definitions). The categories and codes were manually applied to the transcripts of both groups.

The analysis identified many issues in Australian CRE practice. Some were raised in both focus groups and may be considered generally relevant. Other issues were raised in only one focus group. While specific to a particular organisation type (corporate or government) they collectively enlarge our understanding of the issues.

The following discussion presents one key outcome, namely the interaction between property management and financial, or business, management.

Discussion

The link between financial, or business, and property related aspects was one of the many CRE management issues noted in the analysis. This was evidenced in the responses to trigger statements on the following topics:

- Making CRE more strategic
- Decision-making in CRE
- Skills needed by CRE managers
- Outsourcing
- Organising CRE management into a CRE unit

Focus group participants noted the influence of financial, or business, as well as property considerations in each of these areas.

From the analysis it is apparent that the two realms conflate into a body of skills and knowledge that fuses property and financial aspects.

CRE and strategy

The strategic benefits of CRE and the linkages between financial aspects and real estate were clearly noted. The strategic emphasis placed on the provision of corporate property shows that the areas of business and property are fusing into a single body of knowledge. Participants noted for example:

'So the impact's very, very large, but more particularly it (CRE) can impact significantly on the ability of the business to deliver its business aims. That is most evident at the retail end. So roughly around the world we've got a couple of thousand shops which are going to transform themselves very, very significantly over the next couple of years and the strategic influence as well as most of the benefits flow directly out of the real estate. So real estate can't, its no longer viewed as a sort of passive item of production. It is very much a group of assets and expenditure that are quite crucial to the business needs of the corporation as distinct from giving it a roof over its head.'

'I mean, it's the bit about them being a strategic class of assets. If they're not sort of sitting very close to the heart of the corporation's financial strategies it's highly unlikely to be successful.'

'... the parts of the business strategically that we relate to, there's obviously a capital piece, that's getting the cost of capital right across a whole spread of assets including real estate; there's a finance and investment piece; there's a retail piece'

'... how Corporate Real Estate contributes either to the cost of doing business, or to the bottom line in generating revenue, like having the right location to attract customers or having the right layout of a shop, to attract

customers versus what's the cheapest way that we can house our businesses'

The corporate group identified that a strategic environment includes both financial and customer orientations in the property elements. The government group added that service delivery, governance and political considerations are also part of their strategic environment.

'... community expectations have been raised in many respects. They expect information about how well services are being delivered, ...'

'I think ultimately, at the end of the day, many of those decisions, policy decisions, are essentially political ones, despite the best will in the world of wanting to have logical, strategic plans, those decisions will be made on individual issues and individual assets in response to pressures of the time.'

The influence of political considerations does not always lead to good strategic management, but this was certainly described as being part of the government environment.

The strategic aspects of CRE can be consolidated as follows:

- Capital
- Finance
- Retail (provision of customer interface)
- Service provision
- Governance, or political policy

Financial aspects are now elevated in importance above traditional CRE management requirements. This is because today strategic considerations make successful property strategy conditional on alignment with organisational strategy. There used to be little need for property managers to acquire financial knowledge, because property did not have this proximity. But in today's strategic

environment, financial knowledge has to be added to particular knowledge of property.

Decision-making

It is in decision-making that the confluence of the two streams in CRE is most clearly identified. Strategic CRE management requires business and property aspects to be aligned. Participants expressed that the preferred methods for making CRE decisions consisted of, in a parallel process:

- The preparation of the business plan for the proposed action; and
- A separate property case that includes all aspects of the property costs – weighted cost of capital, fitout costs and the like – and meets the objectives of the action. In this way property supports business decisions.

'... there tends to be a business component and a real estate component. So, what we do in our place, is take decisions that way. The business said that this is something that it needs to do which has certain benefits and costs, and then the real estate decision that sits across the back of it, which also has benefits and costs.'

'We separated the property or the CRE decisions from the business decisions in the first instance, so the business will do a business case and we will provide the market based advice in terms of what it would cost them to secure the facility on the, you know, from the market place and the cost of their fitout and all those sorts of things, and they make a business decision whether it stacks up.'

'...making the cost of, and importance of that community infrastructure transparent, I think is probably one of the key steps in becoming more strategic ...'

Decision-making requires all the issues to be clearly and coherently established prior to the decision being made. CRE

management can transparently provide choices that support this process. Only when this clarity is achieved, can the business and property cases be brought together in a comprehensive decision.

CRE skills

The need for CRE management to have business and property skills has been highlighted in the discussion about CRE decision-making.

The focus groups clearly indicated that process management, lateral thinking and organisational awareness are all important skills in CRE management

'I think our emphasis is really: can they manage a process?'

'A good corporate real estate manager does need to be strategic, does need to have those strategic planning skills but you've also got to be pretty pragmatic, because you're dealing in a very pragmatic environment.'

'If they can't get up there in terms of having, you know, vision and energy and all those sorts of things they're not going to make it irrespective of their particular background.'

'... a really competent CRE manager, ...has got to be able to deal with the transition from the vision to the implementation.'

'When I think of the heavy hitters that I watch around the world they've come up, you know, with backgrounds all over the place. I don't think somebody necessarily has (to have) a bricks and mortar background or finance background.'

Originating technical skills were not considered to be important. Rather, emphasis was placed on the capacity to develop the required skills in areas other than a manager's originating background.

This is emphasised by the fact that organisations that have historically been focussed on internal, technical aspects (a characteristic of government organisations, but not unknown in corporates either) are now requiring their employees to shift from being operational doers to being strategic, organisational managers.

'You need people to manage the outsourced process and it's all down to those people who were the doers in the past becoming, all of a sudden, managers. Unless they can make that leap from doing, being the property manager, to all of a sudden become a strategic thinker and a manager of a whole global area they're going to fail.'

An understanding of business was noted as crucial to success.

'But the more they (CRE managers) understand business, and business stream and how the business is driven, the higher the degree of success they're going to find in terms of going further in CRE because you can't be just one or the other.'

This demonstrates that property managers need an understanding of business, consistent with the point made in the earlier discussion of the strategic environment.

In addition, part of the CRE skill-set in practice was identified as the ability to mediate between and communicate with higher management and operational levels.

All these – the need to communicate, the move to strategic management, and the development of skills – point towards CRE management practice requiring a hybridisation of knowledge from both property and financial realms.

Outsourcing

Outsourcing was accepted as a fact of life in the present business environment. However, the retention of strategic property management in-house was specifically noted:

'I think strategic capabilities have to be retained in house. And the form of that, I think, can be all over the place.'

The ability of the organisation to meet its strategic ends in an outsourced form was questioned, as the outsourcing of strategic direction was felt to compromise the integrity of the organisation.

In examining the organisation's form, it was noted that it had 2 distinct parts - an organisation-wide management function and an operational-technical one. CRE management, as previously noted, spans both elements. In the extreme case, where all CRE functions are outsourced there are still specific outsource-contract administration and process management tasks that require the retention of some property knowledge. The specificity of this knowledge is difficult to graft onto senior management's generalist role, thereby providing additional evidence of the value in maintaining some form of property management in-house.

External service providers can provide particular services, so called out-tasking, but the retention of internal strategic CRE, process management and property related knowledge was noted as contributing to the integrity of the organisation.

Doubts about the availability of the requisite skills and advice in the service provider market raised questions about achieving strategic outcomes suitable to the specific organisation. Because of that unavailability there were doubts about the success of outsourcing all CRE functions. Also, questions about the integrity of the organisation in an outsourced form was raised.

Service providers certainly have specific financial, property management and real estate transaction skills. Plenty of these skills are available, even if they are largely historical, relying on either financial or property skills. The conflated hybridisation

of knowledge and skills applicable to strategic CRE management is much rarer.

'We have this, I think very pedestrian position by Corporate Real Estate advisers about what is the best practice and for anybody to have the notion that best practice is [to] get all the real estate off the balance sheet or sell off real estate does not understand the very strategic nature of Corporate Real Estate and how you can use Corporate Real Estate to increase shareholder value and increased corporate competitiveness.'

'I don't think that the transition in the managers, or the groups, that want to take over this strategic end service delivery management, are out there yet. A lot of them are still real estate agents who collect the rent. Others are facility managers that maintain buildings. A lot of them haven't made that connection that there are two sides to the whole function, where you start to look at the total picture.'

The CRE unit

The value of a strong CRE unit surfaces in several of the areas discussed above, eg the hybrid skill-set required, and in the need for in-house administration capacity between the management and operational levels. It is also evident in the doubts about service providers having appropriate strategic CRE skills. All these justify the existence of a CRE unit.

Expertise in strategic asset management developed by CRE units was noted by both focus groups as being applicable in other parts of the organisation, such as information technology assets and property branding. The transfer to other areas entails an educative role about strategic asset management, both at senior management level and at the operational level.

'I'd add that we are trying to raise the awareness within the corporation of how

Corporate Real Estate contributes either to the cost of doing business or to the bottom line in generating revenue.'

Acting as a go-between for different levels of the organisation again characterises the dual nature of CRE management. It needs to be competent in and comfortable with both knowledge areas to which it is required to relate.

Conclusion

Australian CRE management issues are many and diverse. However, one of the key findings of this research is that CRE management spans the dual realms of financial, or business, and property related knowledge. The practice of CRE management exhibits this hybridisation in five key areas.

Firstly, strategic management of corporate property occurs through CRE management being located close to the financial heart of the organisation.

Secondly, decision-making requires that business, or financial and property related decisions are each soundly established before being brought together.

Thirdly, as CRE management bridges business and property realms, the skill-set of CRE managers is a hybrid of both. A manager's originating technical background could be either property, or financial. This is not the issue. What is of more concern is that the individual has the capacity to acquire the skills and knowledge that they do not already have.

Fourthly, because of the unique nature of the skill-set, concern exists about the availability, in the service provider market of the requisite skills for the strategic management of real estate. Certainly there are specific financial, property management and real estate transaction skills available, but the hybrid knowledge applicable to strategic management is rare.

Finally, if CRE management is housed in a strong CRE unit, it provides a receptacle for the knowledge particular to CRE management. As a consequence the hybrid skill-set has the capacity to span both the business and operational levels of the organisation.

This paper presents only one aspect of the ongoing research program exploring current attitudes and beliefs about CRE management in Victorian organisations. Other aspects of the practice of CRE management that emerged from the focus groups will be presented in other forums, as will other research into CRE's contribution to organisational competitiveness, implementation of CRE practices in Australia and the particular competencies required for CRE management. The last issue is especially interesting in light of the hybridisation of skills that this paper has identified.

The area of CRE research in Australia is just opening up. There are many opportunities for research. As a beginning, replication of studies carried out elsewhere to validate findings for Australia awaits researchers. Other potential areas, such as changes to workplace environments, the use of alternative workplace practices, and the impact on property suppliers have not begun to be examined in Australia. In addition, the impact of electronic commerce is an area that will have global implications for corporate property.

The role of CRE in non-corporate organisations such as local, state and federal governments and the value that their property holdings have in their operations is yet another example of a potentially rich area awaiting those wishing to explore CRE research.

This paper is, hopefully, just a part of the beginning.

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Appendix - Codes

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| Code Label | Code | Definitions |
|-----------------------------|--------------|---|
| Strategic Management | SM | |
| Commitment | SM-COMM | Commitment to strategic CRE practices supported at the highest level of the organisation |
| Property Investment | SM-INVEST | Using property as a strategic investment |
| Pro-active | SM-PRO | Pro-active in applying, seeking strategic opportunities Informing other functional areas of the organisation regarding benefits of strategic CRE practices Leadership of the organisation in terms of CRE principles Acting on a vision of organisation's future |
| Alignment to business goal | SM-BUS/ALIGN | Understanding the corporation's core business, its competitive advantages, and integrating the real estate decision with corporate goals Bottom line is to increase shareholder value and to obtain long-term objectives of the corporation Aligning CRE decisions with the organisation's business needs |
| Reviews | SM-REV | Reviewing, periodically, the relationship of CRE to the organisations goals, structures, and <i>modus operandi</i> |
| Organisation | ORG | |
| Organisation dynamic | ORG – DYN | Inter-relationship between different parts of the organisation (involving CRE practices) |
| Organisation structure | ORG – STRUCT | Reference to the organisation's structure |

| | | |
|--------------------------------|----------------|--|
| Independent CRE unit | ORG – UNIT | CRE is organised as a wholly owned real estate subsidiary, a corporate entity which is profit oriented and motivated |
| Change | ORG – CHNG | Changes within the organisation (not necessarily CRE related) Changes in structure, processes, procedures, etc |
| Reporting | ORG – REPORT | Reporting within the organisation |
| Performance Measurement | PM | |
| Type of Metrics | PM – MET/TYP | A type of metric Reference to any type/s of metric |
| Number of Metrics | PM –MET/NO | Reference to the number of metrics used |
| Business Plan | PM – BUS | Measurement against the organisations business plan |
| Market comparisons | PM – MARK | Measurement against the market place Use of market valuations to measure property portfolio |
| Benchmarking | PM - BMARK | Benchmarking practices and procedures |
| Service measure | PM – SERV | Measurement of service provision to customer, client, etc |
| Intervals | PM – INT | Intervals at which performance measurements are taken |
| Financial | PM – FIN | Financial performance measure |
| Site Selection | SS | |
| Location | SS – LOC | Location of real estate is important to the organisation’s business |
| Ownership method | SS – OWN | Method of ownership of the real estate asset – ie freehold, lease, etc |
| Strategic | SS – STRAT | Location is strategic to the organisation’s business, or is an essential asset for community or operations |
| Financing | FIN | |
| Methods | FIN – METH | Method of financing the real estate assets |
| Measurement | FIN – MEAS | Measurement of financial criteria |
| Asset comparison | FIN – ASS/COMP | Comparing performance of organisation’s different types of assets |
| Role of capital | FIN – CAP | Role of capital on the balance sheet Source of capital to finance local government real estate assets. |
| Maintenance of asset | FIN – MAIN | Costs, financing arrangements for maintenance of the asset |
| Relationship to asset | FIN – ASS/REL | Relationship between financing method and the asset type and ownership method |
| Outsourcing | OS | |
| Management | OS – MAN | Management of outsourcing arrangements |

| | | |
|------------------------|-------------|---|
| Cost implications | OS – COST | Cost implications of outsourcing arrangements |
| In-house tasks | OS – IN | Organisational tasks retained, or required to be retained in house |
| Management skills | OS – MAN/SK | In- house management skills required |
| Models | OS – MOD | Types of outsourcing arrangements and structures |
| Decision Making | DM | |
| Real estate component | DM – RE | Assessment of real estate priorities, information |
| Business component | DM – BUS | Assessment of business case for asset |
| Methods | DM – METH | Use of real estate and business assessments to make a real estate decision Methods to make decisions |

| | | |
|---|---------------|--|
| Skills and Competencies (in-house) | SK | |
| Finance | SK – FIN | Financial/business skills |
| Real estate | SK – RE | Real estate skills |
| Process management | SK – PM | Management of CRE processes Balances between competing priorities – technical, financial, etc Has a ‘corporate’ view |
| Capacity to develop | SK – DEV | Capacity to develop further skills and competencies as required |
| Strategic Planning | SK – STRAT | Strategic planning skills |
| Technical | SK – TECH | Technical skills, incl. Bricks and mortar, professional technical skills as opposed to real estate skills) |
| IT skills | SK – IT | Understanding of IT requirements in modern work places |
| HR skills | SK – HR | Understanding of Human resources requirements in modern work places |
| Workspace | WS | |
| Specialist design | WS – SPEC/DES | Use of specialist designed work places/spaces |
| Requirements | WS – REQ | Requirements of workspaces |
| IT | IT | |
| GIS/LIS | IT – GIS | Use of a geographical or land information system to hold asset data |
| System integration | IT – INTER | Integration of IT/data systems |
| Data collection | IT – DATA/COL | Collection of real estate data into data bases |
| Data base | IT – DATA/BSE | RE database (not necessarily GIS) |
| Customer Focus | CF | |
| Customer surveys | CF – SURV | Surveying customer’s attitude’s satisfaction |
| Community expectations | CF – COM/EXP | Expectations of community (Local government) regarding real estate, service delivery, etc |
| Community benefit | CF – COM/BEN | Benefit to community |
| Governance | GOV | |
| Administration | GOV – ADMIN | Use of CRE practices to provide quality decision making information to organisation’s government |
| Policy | GOV – POLICY | Policy setting by organisation’s government – board, council, etc |
| Decision making | GOV – DM | Decision making by organisation’s government – board, council, etc |
| Future Research Issues | FRI | |

