“Managing key resources and capabilities: Pinpointing the added value of CREM”

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Abstract

In contrary to the external focus of the corporate strategy up to the 1980s corporations are increasingly focusing on managing the internal corporate resources and capabilities. The resource based view - one of the main streams in organizational economics - stresses the importance of resources and capabilities to the performance of an organization. As a result of the changing relations between the corporate centers and operating companies and an increasing trigger to outsource non-core activities, staff and supporting functions such as corporate real estate management are urged to prove their added value to the bottom line of the corporation. The resource based view and the resulting concept of synergy is the basis for an analysis of the changing role of corporate real estate management (CREM). Based on the findings of case-studies - performed as part of the Ph.D. thesis in real estate management - an overview is presented of implementations of horizontal and vertical synergy in managing corporate real estate. The focus of this paper, parallel to the objectives of the thesis, is to describe the evolution of real estate management related to the growth of multinational corporation and to pinpoint the added value of CREM in today's corporate setting.

Keywords:

Corporate real estate management, synergy, added value

I. INTRODUCTION

Although the activities of corporate real estate management (CREM) can be dated back to the beginning of industrial and commercial activities, from both an academic and a professional point of view CREM is still in its childhood years. Up to now the majority of the academic attention towards buildings has been from either an architectural or economic point of view. Starting of in the beginning of the 1980s, the attention peaked in the early nineties as a result of the publication of the first of a series IDRC reports ‘Strategic management of the Fifth Resource’. Although CREM has gained increasing attention in the last decade, the majority of research is limited to either surveys, prescriptive articles, or valuation articles. Besides being primarily based on North-American success stories the majority of research efforts has a strong financial orientation and views real estate mainly from an investors point of view. The profound impact of the corporate setting on the corporate attitude towards real estate and on the organisational implementation of CREM is however hardly addressed in the real estate literature.

Transitions in the corporate attitude towards internal service providers, triggered by changing relations between corporate centres and operating companies, and by a professionalisation of the real estate market, changed the traditional role and position of staff-departments. Instead of acting as a monopolist, CREM departments have to position themselves against outside commercial service-providers. Only decades ago multinational corporations, although not professionally active in the real estate industry, maintained engineering and architectural departments in some cases employing more than thousand employees. Currently departments are urged to identify their competitive advantage, and to provide services/products which deliver an added value. Based on the findings of multiple cases an effort is made to pinpoint the added value of CREM. This paper provides a description of both the triggers and preliminary findings of a thesis currently in progress at the Delft University of Technology, called: “Corporate Real Estate Management in Multinational corporations”.

II. A TRANSFORMATION OF A DISCIPLINE

Up to the 19th century real estate was either merely used to accommodate people and their activities or to express the wealth of those who ordered the construction of the buildings. The rapid growth of industrial and commercial activities in the beginning of the 20th century and the consequent need for buildings resulted in increasing amount of capital allocated in real estate. While accommodating the early industrial activities was merely a responsibility of the owner of the corporation, in the beginning of the 20th century corporations started to establish staff and supporting departments involved in managing the corporations real estate. The lack of alternatives forced corporations to control and own both the buildings and the supporting real estate services. An example of the centralized attitude of the corporations is the following quote of Anton Philips one of the founding father of Royal Philips Electronics in 1929:

> *"it has appeared desirable to co-ordinate and manage all matters relating to purchasing and renting real estate, renovations and construction, outside of Eindhoven, in one centralised position"*

The objectives underlying the foundation of the departments were:

- control construction activities, both at technically and financially;
- guaranteed availability of skilled employees;
- creating and maintaining a corporate image with regard to the architecture of the buildings, and
- avoiding and reducing of corporate taxes.

By the time of World War II industrial corporations had evolved into truly multinational corporations. Corporations as Philips Electronics, Royal Dutch Shell and Unilever operated national subsidiaries in more than 40 countries all over the world.

Until long after World War II the majority of the corporate real estate activities was controlled from out of the home country, and was mainly involved in guiding the constant need for additional accommodation. The continuous corporate growth and increasing geographical spread of the business activities between 1960 and 1970 resulted in an increasing diversity of the portfolio both in product and geographical diversity. Responding to the expansion of the organisation, corporations transformed their traditional functional structure into a more geographical oriented structure. Parallel to the structural turn-around, corporations started to decentralise responsibilities from corporate headquarters and central staff departments to

national organisations and operating companies. This shift of authority led - in many a case - to a confrontation with the urge to provide an added value. The necessity to provide an added value was enhanced by the emergence of professional real estate consultants, and the growing corporate desire to allocate their scarce (financial) resources to core activities.
In was not until the end of the 1960s that the early professional real estate agents and consultants emerged in the Netherlands. The reduction of government subsidies on housing and the emergence of British real estate investors triggered the Dutch commercial real estate market. This ended the necessity of owning real estate assets. Combined with an increasing corporate demand to focus on the core business activities, the Dutch commercial real estate market started to flourish.

The rising costs of accommodation as a result of the 1973 oil-crises, combined with the introduction of the computer and information technology in the business processes, and globalisation of markets, triggered the managerial attention for real estate and real estate services. The corporate recession in the beginning of the 1980's resulted in further pressure on staff and support departments as real estate management. Paralysed by trends as back-to-core-business, downsizing, lean-production, outsourcing, or right-sizing, corporations laid off thousands of employees resulting in an surplus of office and production space. The rising vacancy and the consequent decline of market rents resulted in a decrease of both (internal) rental incomes and rate of return on the real estate portfolio.
CREM departments had to rub their eyes and wake up. Facing the changes in the corporate environment, real estate has to be managed, just like other corporate staff and resources. Real estate is to be managed as a corporation's fifth strategic asset, after employees, capital, technology, and information. The transition in the demand for accommodation and the changes in the real estate market have contributed to the recognition of the financial and added value of real estate. The downside of the recognition of the cost of real estate is however that corporations start looking for alternative manners for organising the supporting activities
Parallel to the changes in the focus on real estate, the focus on interest in the analysis of competitive advantage shifted at the end of the 1980s towards the internal aspects of the corporation. Competitive advantage was seen as depending less upon corporate choices in market positioning and more upon the exploitation of unique internal resources and capabilities. The major challenges for corporate real estate management is to prove the added value of real estate to the corporation. Faced with a corporate strive to withdraw its activities back to the core-business, functional departments like corporate real estate management are urged to justify their in-house presence. They have to prove that they are at

least as competitive as outside service-providers. Although cost-efficiency is often regarded as being the most important competitive advantage, other elements of added value might prove to be at least as effective. As Michel Porter (1996) stated in his latest contribution to the Harvard Business Review: “Operational Efficiency is not Strategy”. Based on the theory of the resource-based-view and the succeeding concept of synergy an effort is made to pinpoint the added value of corporate real estate management. Before identifying elements of added value a brief overview is given of the objectives and research approach of the underlying Ph.D. thesis.

III. MANAGING A CORPORATIONS REAL ESTATE PORTFOLIO

The impact of the changes in the corporate setting and the absence of research focusing on the impact of corporate changes on the role and position of the CREM department have been the most important elements to start of with this Ph.D. thesis. The first objective of the thesis “Corporate real estate management in Multinational Corporations” is to relate the evolution of corporations from small family run enterprises to multi-business and -country corporations to the needs and organisational implementation of corporate real estate management. The second objective focuses on the way real estate resources and capabilities are applied in order to contribute to the corporate performance. The objectives are two-folded:

1. *to acquire insight in the evolution of corporate real estate management in relation to the transformation and transitions in the strategy and structure of multinational corporations.*

2. *to pinpoint the added value of corporate real estate management and identify the impact of corporate characteristics on the nature of the added value.*

Case studies	1900-1940	1940-1980	1980-2000	
Individual Corporations				Analysis of individual case
	Over-all analysis per time-frame			CREM in MNC

Figure 1: Analysis of the case studies

Fulfilling the first objective provides insight in the relationship between changing characteristics of the multinational corporation (MNC) and the needs for corporate real estate management. With regard to determining corporate characteristics a distinction is made in three categories: structure, strategy, and synergy. Following the concept of the resource based view characteristics of the MNC are identified which are of influence on the corporate attitude towards managing core capabilities and resources. The evolutionary relationship is consequently analysed on the basis of the defined characteristics. Focusing of three adjacent time-frames the analysis provides a description of the evolution of the CREM function within multinational corporations.

The second objective focuses on the crystallisation of the concept of 'added value' and on relating the nature of the concept applied to the corporate setting. The resource based view and the consequent concept of synergy provide a theoretical basis for determining the added value within a corporation. The implementation of synergy in corporations is used as starting point in the attempt to pinpoint the added value of CREM. The nature of the added value delivered by CREM is ultimately related to the current corporate setting.

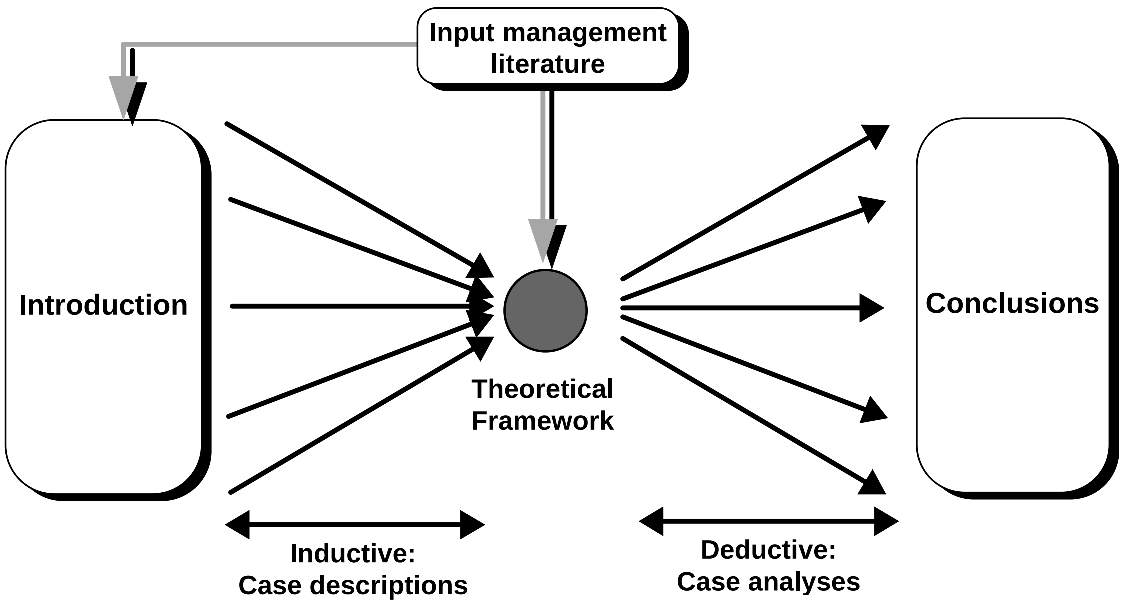

Figure 2 Framework underlying the thesis

In order to analyse the relationship between characteristics of the multinational corporation (MNC) and role and position of those departments involved in managing a corporations real estate portfolio both in time and current, a limited number of cases is reviewed in-depth. All of the selected corporations have been founded in the beginning of the 20th and have evolved in time to become corporations listed in the Fortune Global 500. Each of the corporation has been faced with either major mergers, acquisitions or with extensive reorganisations, and obtains at least thirty percent of the revenue outside the home-country. The choice for multinational corporations in stead of domestic corporations is based on the impact of geographical spread and diversity of business activities. Based on material available in corporate archives, interviews with in-house experts, and publicly available information, an analysis is made of each of the case studies.

Although the illustration the hypothesis are based on Dutch corporations, the trends and issues facing the CREM discipline are recognisable all over. In the same way the impact of the changes and the consequent responses of the corporations with regard to managing the corporations real estate portfolio may also provide general lessons.

IV. USING THE RESOURCE BASED VIEW TO ESTABLISH A THEORY FOR PINPOINTING THE ADDED VALUE OF CORPORATE REAL ESTATE MANAGEMENT

Given the setting of this thesis, one of the main elements with regard to establishing a theoretical background is the discipline of strategic management. In the beginning of the eighties the majority of researchers in management studies were focused at the industry analysis framework associated with the work of Michael Porter and Henry Mintzberg. Strategic management research focused on the structure of the industries within which a firm operates as to explain heterogeneity in firm performance. During the late 1980s and early 1990s the focus on interest in the analysis of competitive advantage shifted towards the internal aspects of the firm. Whereas in the industry analysis framework, the firm is treated as essentially a black box, strategy researchers are now turning towards an approach that places emphasis on the firm’s endowment of capabilities for understanding the sources of sustained competitive advantages. Resources and capabilities are seen as the principal basis for strategy and the primary determinants of firm profitability. Even advocates of the positionings approach are now addressing the fact that strategy should rest on unique activities, and that operational effectiveness is merely a necessary part of management.

The resource-based view (RBV) focuses on the resources and capabilities of a firm as its primary unit of analysis. Although real estate is often not explicitly incorporated in the various overviews of corporate resources and capabilities, real estate is undeniable one of the physical resources of a corporation. In line with the RBV, the hypothesis underlying this thesis propose that management of corporate real estate can provide an added value to the bottom line of the corporation.

One of the concepts that has been at the core of the RBV is the concept of synergy. Although not using the exact word Edith Penrose (1959) addressed two basic forms of synergy: asset sharing and asset transfer. The idea underlying of synergy is represented by various notions as ‘related diversification’, ‘corporate coherence’, ‘parental advantage’, and ‘core competence’. The synergy concept stresses that advantages are created when economics of scale and speed are combined with administrative co-ordination. Synergy focuses on co-ordination of existing structures and on how managers can optimise interrelationships between parts of an organisations [Anderson & Matsgård, 1996]. The following table depicts some of the many classifications of synergy.

Authors	Classification of synergy
Ansoff (1965)	• sales synergy • operating synergy • investment synergy • management synergy
Porter (1987)	• portfolio management • restructuring • transferring skills • sharing activities
Goold, Campbell, and Alexander (1995)	• stand-alone influence • linkage influence • functional and services influence • corporate development activities

Table 1: Classifications of synergy

It is clear from the above reasoning that an important role in creating and maintaining synergies is set aside for corporate staff and support departments, including CREM. As a result of the transformation of the focus on the corporate competitive advantage an increasing interest is arising for the added value of managing a corporation's real estate portfolio.

The impact of real estate on the corporate balance sheet is a evident expression of the (financial) value of real estate. Nourse and Roulac (1993) argue that real estate is 25 percent or more of corporate assets, and occupancy costs represent 40% to 50% of net operating incomes. Financial and economic criteria are however no longer the only basis for determining the added value of corporate real estate. In contrary to the traditional transaction orientation real estate managers have to focus more on the interests of the corporate stakeholders. Based on the theory of the RBV and the consequent concept of synergy, and on the results of case studies a classification can be made of 'value adding' products and services with regard to CREM. Besides being able to respond more accurate to the demands of the core business activities the elements may even provide departments with a competitive advantage over outside providers. Similar to Penrose's distinction in the nature of corporate synergy a distinction can be made between in the nature of CREM products and services.

Resource sharing	Capabilities transfer
	
1. Economies of scale in acquisition of products and services 2. Alignment in use and management of real estate and real estate services 3. Providing qualitative services for competitive prices	1. Knowledge of the business and management processes 2. Collection of scarce expertise 3. Risk sharing 4. Confidentiality on and availability of information 5. Formal and informal network 6. Speed of (trans)actions

Table 2: A classification of value adding products and services

The extend to which the elements of added value are implemented within organisations depends however largely on the specific corporate setting in which CREM is operating. The diversity and fragmentation of the corporation, influencing the possibilities to create or maintain economies of scale and scope, determines the complexities of managing a corporate real estate portfolio.

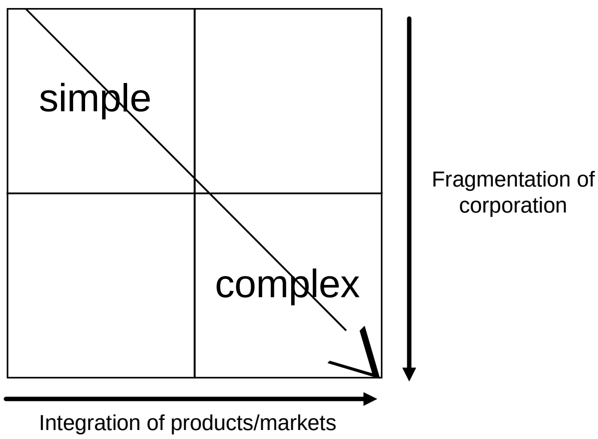

Figure 2: Increasing complexity of corporate real estate management [Krumm, 1996]

Complex organisations with a high diversity in products and markets will often be unsuitable setting for a centralised CREM perspective.

Centralising real estate activities in these organisations will create enormous tension between the corporate strive for synergy and the demand for autonomy and flexibility in the operating companies. The organisation therefore has a choice between two organisational forms: a decentralised real estate unit or a centralised but geographically dispersed real estate unit. By decentralising the real estate responsibilities the advantages of economies of scale are lost. By dispersing geographically, a good balance can be found between the needs for flexibility and the advantage of organising real estate centrally. In extreme situations the CRE manager is forced to limit activities to a more advisory role. Less diversified organisations might benefit from a centralised approach to CREM.

In either case, the key word is customisation. CREM has to be aware of and understand the needs of its stakeholders and their demands. As a result the role and position of CREM and consequently the nature of added value will vary between corporations.

V. PRELIMINARY CONCLUSIONS: PINPOINTING ADDED VALUE

During the various phases in the life cycle of the corporations, the need for staff and support departments evolved. While the needs with regard to real estate was originally primarily focused on the assistance in the continuous need for accommodation, nowadays the prime focus is on outsourcing services and reducing the impact of real estate on the corporate balance sheet. In order to continue to provide an added value to the internal clients within a corporation, the real estate management departments have to be aware of three key elements:

- their own capabilities and resources,
- the changing needs and authorities within the corporation,
- the context and markets in which the corporation operates, and
- the presence of a corporate awareness of products and services available within the staff and service departments

In order to retain a position in the corporation departments have to analyse their current products, services, and relations with clients. Insight in their own capabilities and resources is essential in order to be able to understand and respond to the needs of the incorporate clients, and consequently for the continuation of playing a key role and position of corporate real estate management within multinational corporations.
The Ph.D. thesis “Corporate Real Estate Management in Multinational Corporations” focuses on the transition in the need for CREM activities and on the consequent impact on the organisational implementation of the departments involved. At the time of the conference the process of writing the dissertation is expected to be almost completed. The upcoming six month will be consummated by external reviews of the dissertation which will hopefully lead to a completion in the late spring of 1999.

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