Agile companies turn to outsourced office space to cut overhead costs.

executive white paper

Regus®

Matching workspace with business needs for flexibility and cost-control.

By Bob Gaudreau
Executive Vice President

The most powerful validation for the need for outsourced office space is the glut of sublease space that has flooded cities across the US. Current vacancy rates are only two percent lower than during the recession that gripped the nation in the early 90s. The consensus among real estate analysts and experts is that the commercial real estate market may not recover quickly. So what has gone wrong?

Businesses failed to effectively align their business needs to their property needs. Previous performances based upon the economic prosperity of the 1990s did not serve as an accurate forecasting tool. When the economic boom turned to bust at the end of 2000, companies needed to quickly alter their business plans to adjust to the new economic landscape. One of the fixed line items that could not be changed on the balance sheets were the long-term leases to conventional office space. As a result, companies are now enduring the reality of poor real estate planning and are saddled with thousands of square feet of excess office space they don't need, yet have to pay for. Sublease space is typically offloaded at a discount and businesses lose money on the deals. As companies built-out and occupied conventional office space they incurred high capital expenditure costs. If that space is vacated prior to the lease end date, any unamortized capital expenditure is required to be written off immediately. This adds depression to a profit and loss account already struggling with restructuring. And, as companies grapple with today's economic uncertainties, their rigid property portfolios have turned into a financial drain.

To combat mounting fiscal challenges, companies have audited all business functions from HR to IT and have slashed their variable costs to the absolute minimum. Until recently, businesses continued to blindly commit to their fixed costs, which included real estate expenses because no alternative solution existed. Now, with the emergence of outsourced office providers, organizations can aggressively cut real estate costs, restructure their portfolio to include a beneficial mix of long and short-term commitments and gain flexibility that will help them successfully manage change.

Competitive Advantages of Outsourcing Office Space

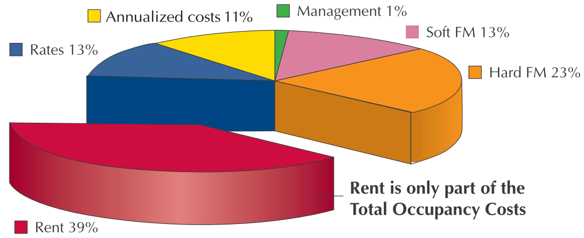
1. **Fixed and competitive pricing**
   No start-up costs, tax, depreciation, etc.
2. **Consolidate spending**
   Get greater discounts based on aggregate global expenditure.
3. **De-risks your portfolio**
   Easily transfer locations as needed; only pay for the space you use and when you use it.
4. **"Best in class" IT and workspace platform**
   Put systems into place once and replicate throughout your portfolio globally.
5. **Strategic global portfolio review**
   Enables you to respond quickly to the needs of your local teams.
6. **One global agreement**
   Eliminates barrier to entry and complies with regional rules and regulations.
7. **Highly trained local teams**
   Indigenous personnel speak local language and are aware of customs and regulations.

Target: Total Cost of Occupancy

Total Cost of Occupancy is the second largest fixed line expense a company must incur. Streamlining Total Cost of Occupancy, an all-inclusive dollar amount illustrating what it costs a company to "house" one person at one workstation, has become the impetus behind companies partnering with outsourced office providers.

Companies who outsource their office space automatically reduce Total Cost of Occupancy because they can:

- Craft the right mix of long and short-term property commitments so that sublease space = 0.
- Slash costs from their second largest fixed line item – Total Cost of Occupancy.
- Eliminate up-front Capital Expenditures and redirect that money into propelling their core business forward.
- Leverage the provider's established infrastructure (IT platform, office equipment, furniture).



"A national survey of Total Office Cost". (Axcell, Proctor & Fennel - City University Business School Febuary 2001)

- Share with its co-tenants on-site resources (support personnel, common areas).
- Pay only the services they use (administrative duties, connectivity package).

A study conducted by the Gartner Group and MIT, entitled, "The Agile Workplace: Supporting People and Their Work" suggests that the trend toward office outsourcing will become part of a company's overall strategic plan. Enterprises will outsource their real estate requirements as a means of mitigating financial and property risks as few corporations can predict their ongoing workspace costs with certainty. The study goes on to infer that outsourced office providers are helping companies tear down the pre-existing silos while guiding them toward a cross-functional, holistic view of their business.

"Businesses are continuing to take a holistic view of the total cost of occupancy. They will rely on total cost calculations to reveal the true cost of provisioning workers to make space, technology and outsourcing decisions."

Cost model exposes opportunities

Regus Business Centres fully expose Total Cost of Occupancy for its clients with development of its SmartSpace cost model. *This proprietary workspace calculator provides a head-to-head dollar comparison of outsourced office space versus conventional or sublease space, using a client's actual numbers.* The model affirms the financial benefits of office outsourcing and empowers companies to make fiscally sound decisions. By streamlining costs, companies can redeploy freed up capital once tied into bricks and mortar and redirect it to other strategic initiatives.

Study: Cost-conscious companies need flexibility

Property portfolios that consist solely of rigid five- and ten-year leases in the current economic climate are completely incongruent with the needs of today's businesses. Why? These agreements contradict the flexibility needed to effectively compete and succeed in the marketplace.

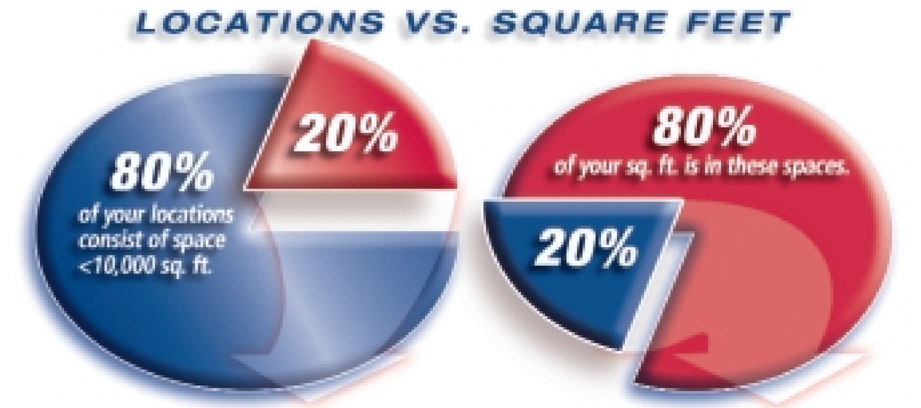
Organizations need the flexibility to seize new businesses opportunities, wherever they may be; need the flexibility to locate, relocate, expand or contract in order to meet market conditions and perhaps most importantly, need the flexibility to bring meaningful cost savings that will profoundly impact the bottom line. With business plans changing regularly, why should companies confine themselves to long-term agreements that may not suit their business needs in the future?

It is anticipated that over the course of the next five years a dramatic period of change will occur in the way that businesses fulfill their office accommodation requirements. There will be an explosion in the number of companies seeking to divest themselves of their own property portfolios and unlock the capital contained in it enabling them to better compete in today's hyper-competitive marketplace.

Pitfalls of Conventional Space

- **High start-up costs. Capital investment including architect fees, legal, decoration (furniture, fixtures, plants, etc), telecom connections and management time.**
- **Long-term commitment (5-10 years average) and often inflexible.**
- **Monthly overheads: Numerous bills - including rent, local taxes, cleaning costs, building insurance, maintenance and utilities.**
- **Variable costs: Personnel costs, reception, telephone bills, IT, postage, copying, etc.**
- **Plus dilapidations and exit costs.**

Aligning Real Estate Portfolios to Meet Location Needs



Fixed Portfolio

- Large Campus
- Call Centers
- Warehouses
- Manufacturing
- R&D Lab
- Country Hubs

Liquid Portfolio

- Branch Offices
- Sales Offices
- Swing Space
- Project Offices
- Overflow Offices

A study recently released by CoreNet revealed the top issues facing top corporate real estate executives:

- Companies need to focus on their core competency and are looking to outsource non-core functions such as real estate.
- Businesses must have flexibility in terms of:
  - Size: the enterprise must be able to upsize or downsize cost-effectively in response to market conditions.
  - Location: A business has a head office in New York today, but requires 12-month project space in London. What property options are available that will maximize productivity while controlling costs?
  - Lease agreements: Must be based on their business needs and not dictated by a landlord.
  - Speed: They need to focus on first to market.
  - Global presence: They need immediate access to the worldwide market place.

Outsourced office space provides businesses with a simple integrated real estate solution combining a company's three largest expense items – people, property and technology. In fact, outsourced office space is more cost-effective for longer periods, for larger numbers of people over a wider geographic spread, according to research by the Chartered Institute of Purchasing & Supply. Companies can save up to 78% on their office space costs by partnering with an outsourced office provider. How? One of the main reasons is that companies can easily (virtually overnight) move into the fully equipped space without any upfront capital expenditures.

And, time is money. A simple one-page agreement circumvents the need for lengthy lease negotiations – saving businesses valuable time. Add to that flexible lease terms and businesses can achieve a newfound agility absent in traditional real estate.

Craft a Sound Portfolio Strategy

Over 70% of all lease transactions are under 10,000 square feet!

An astounding 73 percent of all lease transactions in the US are for requirements of less than 10,000 square feet. Corporate real estate executives are spending an exorbitant amount of time managing these small- to mid-size office space transactions that only make up 20 percent of their square footage. These high-volume or small space transactions are prime candidates for outsourcing.

Outsourced office providers relieve companies of the "brain drain" and the work involved in these transactions while doing it better, faster and cheaper so companies can focus on fewer, but larger transactions.

By outsourcing this "liquid" or flexible portion of their portfolio, companies are then able to re-direct their efforts and concentrate on the high value (80 percent) portion of their portfolio, which comprises transactions in excess of 10,000 sq. ft. and represents their fixed and predictable space. This combination of office space management is the ideal way to balance long and short-term property commitments.

Nokia adapts to changing business requirements

Evidencing the growing trend and benefits in office space outsourcing, Nokia turned to Regus when faced with the challenge of effectively managing its worldwide property portfolio. The real estate department was charged with aligning Nokia's property portfolio to meet not only the needs of their employees, but also of their customers. Their objective was to identify a global provider of office space that would fit their requirements while benefiting from the economies of scale.

The result: Nokia signed a global agreement for the transfer of up to one fifth of its workforce (approximately 10,000) employees to Regus centers over the course of the next five years.

Regus' flexible lease terms, global reach, cost-effective workspace and consistent work platform were exactly what Nokia was looking for in a partner.

"This agreement provides us with both improved operational flexibility and increased efficiency, which will result in a substantial cost saving to our business year on year," says Mark Tamburro, VP, Nokia Real Estate and Facilitates. "We partnered with Regus because they are capable of providing a truly global one-stop-shop solution for our serviced offices. Ours is such a dynamic business that we are constantly having to align our real estate portfolio to meet the needs of our internal and external customers and this agreement helps to meet those needs very well indeed."

Looking ahead: The balanced workspace portfolio

This trend in office outsourcing is increasing on a worldwide scale, as more and more companies examine their cost base and look for more cost-effective solutions to their office accommodation requirements. Current property portfolios that consist solely of traditional lease agreements will hamper the future prosperity of a company.

"The balanced workplace portfolio may have a range of holdings that can support different needs; it must also be periodically reviewed and rebalanced to meet changes in the business environment and corporate decisions regarding capital allocation, financial, property market and business risk," is just one of the conclusions gleaned from the Gartner/MIT Agile Workplace study.

For a significant number of companies, real estate is a local business transaction with global implications. By partnering with a global office provider a CEO or CFO can be assured that every property decision will align with the financial, operational and strategic goals of their business.

Case Study

Nokia Shifts Into Outsourced Space For Global Advantage

In the summer of 2001, Nokia was looking for new and better ways to manage their extensive property portfolio across the world. Nokia had grown at a very fast pace during the previous decade, thanks to their leading edge technology in mobile communications, which made them the global leader and largest manufacturer of mobile phones. The challenge for the real estate department was to align their property portfolio to meet not only the needs of their employees, but also the needs of their customers.

Nokia comprises three business groups: Nokia Networks, Nokia Mobile Phones and Nokia Ventures Organization.

In addition, Nokia has a separate corporate research unit, The Nokia Research Centre. Nokia has sales offices in over 130 countries, research and development in 14 countries, production in 11 countries and a global network of distribution, sales, customer services and other operational units. In total the organization employs around 60,000 people.

Real Estate Infrastructure

Nokia global real estate is segmented as follows:

- Country, HQ, R&D and Manufacturing locations (long term commitment - 5 years +).
- Satellite offices that may be function or project specific (medium term commitment - 2-5 years).
- Temporary offices that would be project specific and would house 1-100 people (short term commitment - 3-24 months.)

Their portfolio is fragmented with many different offices for different projects and divisions, as well as warehouses and manufacturing plants. Early on, the real estate department had identified a number of offices worldwide that it classified as small to medium, anything up to 150 workstations. Some of these offices were in serviced accommodations with different suppliers, and some were in medium-term conventional leases. They set themselves the task of identifying a global provider that would fit their requirements and generate economies of scales, setting up a partnership type of relationship with that provider. As part of a process to tender, Nokia and Regus, the world's leading serviced offices provider, started discussions and negotiations to provide such a service globally.

The main drivers for Nokia were as follows:

1. **Cost savings:** Nokia found that they could save at least 35% of their costs in the relevant locations by moving across to the serviced-office model as outlined by Regus.
2. **Flexibility:** No long-term commitment to leases that are not needed.
3. **Global Fit:** Regus operates in 50 countries, so both portfolios match to an extent.
4. **Price simplification:** Nokia needed to have prices by region, as opposed to country or location. This is something you cannot achieve through conventional leases, as every building and every location has a different price structure. They also wanted to have a number of services and IT packages built into the price. Regus was able to provide this at very competitive rates, given the size and scope of the contract.
5. **Consistency of product:** Regus offices are made to the same standard worldwide with the same services and environment.
6. **IT platform:** All major technology infrastructures, from data to telephony, are already in place as a global platform, secure and up-to-date. The cost saving is important.
7. **Back-office simplification:** By simplifying and centralizing the administrative process, Nokia could free up valuable time to use in other core activities. Regus provides a one-stop-shop concept, managing invoicing, reporting and service agreements centrally.
8. **Speed and ease of delivery:** The ability to move into Regus space with very little notice, and without the hassle of having to look around for space with other providers, thus spending valuable resources.

Regus was able to provide all the requirements, and hence both companies signed a global agreement. The agreement is for a 5-year term and has a potential size of several thousand workstations, as it is expected that up to one fifth of Nokia's worldwide office locations will be transferred to Regus business centres within this time frame. With this strategic agreement, Regus becomes the exclusive global provider of serviced office accommodation to Nokia in all operating regions around the world.

Like Nokia, other multinational organizations are realizing the potential value of this outsourcing model, not only in terms of cost savings, but also time. Freeing up their economic and human resources will place organizations in a better position to focus on their core competencies without unnecessary distractions, such as the ones derived from real estate operations.