Evaluating Office Space Needs & Choices

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Executive Summary

The property market in the UK has changed significantly within the last decade. Both the demand for and supply of office property have particularly been affected. Occupiers' requirements for ever-greater flexibility and the landlords' continued search for sustainable returns have resulted in a range of new property products. Shorter contracts, serviced space and outsourcing have increased the diversity of property solutions available to occupiers.

This research sought to answer the question: *Are occupiers able to assess these new choices and make informed property decisions?* In order to do this, they must have adequate cost data and a framework for evaluation which ensures that they are comparing equivalent situations. If a serviced office is to be compared with a more traditional leasehold situation, the extra costs of fitting-out and servicing the latter must be incorporated into the process.

The research was undertaken in two stages. An extended telephone survey with 48 organisations was conducted to gather general information on data availability, decision-making criteria and processes. This was followed by a focus group which discussed the findings of the survey and its wider interpretation and implications.

The results indicate that there is a problem of availability of and access to occupancy cost data for many organisations. There were a number of organisational constraints to collecting this data including fragmentation of property responsibility and internal reporting structures but there was a desire to overcome these. The need for more comprehensive occupancy cost information was stressed in order to make better quality decisions and externally benchmark performance.

The time horizons for business activity within organisations were often between one and three years. This sharply contrasts with the traditional property contracts on offer. Organisations felt that, in an ideal world, they would like much shorter-term commitments to property but, most importantly, the ability to exit when the space was no longer required. They were willing to pay for this option but there was a lack of clarity over how much or when.

Occupiers also wanted more services to support the running of an efficient office. They were clear that the key to receiving a good service was a well-drafted service level agreement with a provider they could trust. Whether the services were linked specifically to a property appeared not to matter.

The flexibility theme also emerged in the criteria used to select new office accommodation. Ability to exit was ranked third after location and direct property costs. There was some concern that the financial risks associated with property decisions were not fully evaluated and therefore the value of any flexibility to the occupier was unknown.

There appeared to be broad acceptance of the new products such as serviced offices. However there continued to be a perception that these were expensive. The lack of maturity of this sub-market and the limited cost transparency were seen as blocks to further development.

Overall, there are some forces of resistance to the changing market which come from occupiers. The lack of occupancy cost data and an inability to explicitly separate the cost of the services from the cost of the risk transfer for greater flexibility are inhibiting occupiers from evaluating the new property products in a rational way. This in turn is acting as an inertial force on the further development of the serviced space market and other innovative property solutions.

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Introduction

The nature of demand for corporate property is changing significantly as a result of both external economic shifts and the resultant organisational change. This has recently had an impact on the way in which property products are being supplied and packaged within the UK market but this is a new phenomenon. There has been considerable debate in the UK surrounding the disconnect between the needs of occupiers and the property products and related services supplied by the property industry. Much of the blame for this divide has been placed on the providers. It has been asserted that they do not understand occupiers' increasing need for flexibility and diversity. It is contended that property owners, investors and developers continue to demand long-term onerous leases, albeit now reducing to 10 to 15 years, and offer little support or service to their tenants. It is also a common perception in the property market that, to date, providers have not treated their tenants as customers. This is a marked distinction from other markets, for instance financial services, which continue to develop a more responsive supplier/customer relationship.

There is evidence however of change. Increasingly there is a wider range of options available to fill occupiers' varying needs. Serviced offices, private public partnerships, and an increased array of services, even with traditional leases, are now more commonly on offer. The supply side appears to be responding to the challenge by developing new and innovative solutions.

This increased diversity however poses potential problems for corporate occupiers. Although they have called for greater flexibility and choice, they need to have the means of evaluating the options in order to make rational choices. Like any choice, the appropriate solution will differ for each organisation and each circumstance. In some instances a short-term requirement may be best met by an "instant office" solution. In other circumstances a long-term solution is required. The key is selecting the right solution for the right situation.

Therefore, if there is this choice, occupiers need to be able rationally and consistently to evaluate the options available. That requires both data and a methodology for evaluation. Without these, enlightened decisions concerning space are impossible. Although there has been some debate in the valuation literature related to the pricing of shorter leases and options such as rent free periods and break clauses (Ward and French 1997), there has been little investigation of the process by which occupiers evaluate their choices. Similarly although there has been some attempt to investigate customer needs, particularly in relation to relocation (Healey and Baker 1989, Richard Ellis 1994), there has been no attempt to clarify how decisions are made within corporate occupiers.

The aim of this research has been to gain a greater understanding of the way in which occupiers estimate their requirements and assess the options available. In order to gain insight into the decision-making process, a number of aspects were examined. First, any decision about a future requirement will be influenced by the current situation within the organisation. Therefore, the information available on occupational costs for the existing office portfolio was examined in order to gauge the general awareness of total occupancy costs. Secondly, the measures used to evaluate the performance of the existing office portfolio were considered in order to determine the current focus in terms of efficiency. The third aspect shifted the view to gain an understanding of forecasting horizons and lead-times related to the demand for office space within the organisation. The notion was to link this to the way property is procured within the UK market. The final element considered was the process of evaluating new office requirements, examining both the general and financial criteria used in the final selection.

The research was undertaken in two stages. First, a questionnaire survey was conducted by telephone interview during November and December 1999 (see Appendix A). The interviewees were mainly (79%) individuals who were responsible for corporate property within their organisation with just under a quarter having responsibility for facilities management as well. In total 48 individuals agreed to participate from a total of 215 contacted resulting in a response rate of 22%.

The survey respondents mainly came from types of organisations where office space was likely to account for a very high proportion of their total occupational portfolio. In terms of sector, 45% came from the financial and business service sectors and 14 % from the IT, technology and telecoms sector. Just over a quarter of the respondents were from public sector bodies representing both local and central government. The geographic spread of activity of the organisations participating in the survey was likely to be beyond the UK. Approximately one third of the respondent's organisations operated only in the UK while, of the remaining two thirds, the majority were UK-based multinationals (38% of the total). The respondents also represented large organisations with almost two thirds employing more than 5000 employees and over half having a turnover of more than £1 billion. In terms of their office portfolio, 63% had more than 100,000 square metres of space and for half, this was spread across 50 or more buildings or locations. Overall, therefore, the survey represents large organisations with significant office portfolios in sectors which are office space intensive. These are the organisations which would have the most to gain from improved and innovative management of their office space and therefore should be at the cutting edge of current practice.

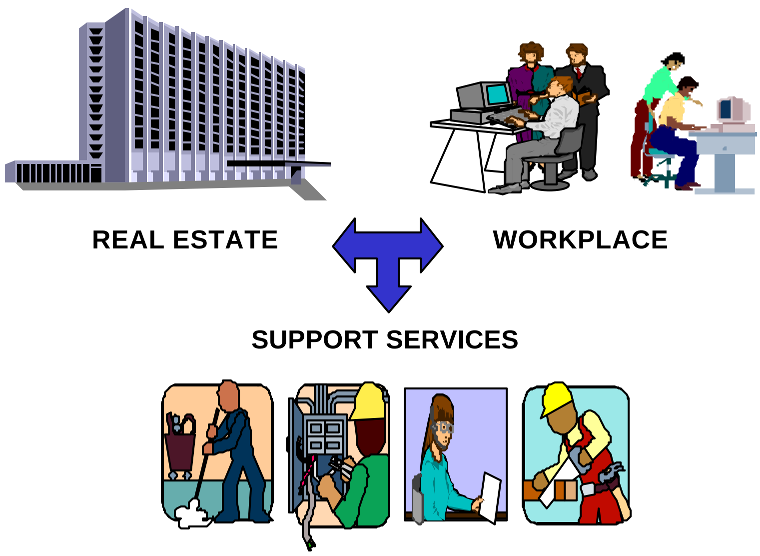
For the second stage of the research in early January 2000 a focus group meeting took place which reviewed the survey results. The aim was to discuss the validity and implications of the findings in order to gain a broader perspective of the issues. Ten individuals took part in the meeting: six from organisations which had responded to the telephone survey and four members of the research team.

This report considers both the survey findings and the focus group discussion in depth in order to answer the question: *Are occupiers currently in a position to make rational decisions when faced with a wide and diverse range of choices?* In order to provide a context for the decisions and to demonstrate the complexity of the current situation, the following section considers the range of products which is emerging on the supply side. This is then followed by an analysis of the occupancy cost data and performance measures currently used by occupiers. The fourth section shows how future office requirements are determined and how, currently, occupiers would like to hold their property. The fifth section reviews the criteria organisations use to evaluate their options and the type of financial analysis undertaken. The sixth section examines the findings from the qualitative elements of the research including both the comments made by the survey respondents and the discussion at the focus group. The paper then concludes with a final section which draws together the key conclusions and makes some observations about the implications of the results for both occupiers and suppliers of office space.

The Changing Demand-Supply Relationship

During the last decade a new way of thinking about office space has started to emerge. A working environment is created by a combination of space, associated infrastructure and services. The infrastructure includes not only the fitting out of the office space but also any other generic equipment required to make the office usable such as the provision of IT infrastructure, telecoms and office furniture. Additionally the servicing of the space also needs to be considered. Both facilities management services and basic office support such as reception, reprographics and post handling must be provided. Increasingly it is recognised that, in order to understand the cost of providing a working environment, a wide range of both capital and annual costs needs to be analysed. Figure 1 shows how the value (and cost) of an office portfolio to an occupier is a combination of real estate plus workplace infrastructure supported by services (facilities management and business support).

Figure 1: Creating and Managing Workplaces



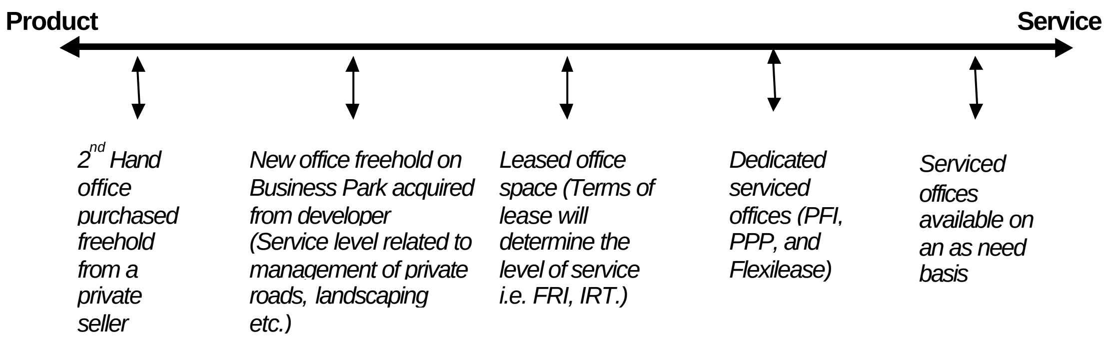
This perspective of an inclusive occupational cost base is probably best articulated by the recently developed OPD Total Occupancy Cost Code (TOCC) (IPD 1999) which seeks to provide clear definitions for each of the key cost headings. (See Appendix B) The rationale for this development has been recognition that not only must occupiers understand their own cost base, but that they also need to be able to compare these costs with other organisations and / or against an index. To date, this has been difficult as each organisation has its own internal management accounting system which defines, collects and analyses data on different bases making comparison invalid. The TOCC also seeks to capture for the first time the totality of occupation costs since most cost analysis has suffered from inconsistency and omission, for instance annualised fit-out costs.

The other issue raised by this analysis is the breadth of elements which needs to be combined to create a working environment. First, it is likely that the range of products and activities which needs to be acquired and managed as part of an operational office will be controlled by a number of departments or groups within a large corporation. Secondly, the drive to focus on core competencies has led organisations to consider which elements of a working environment should be provided, managed and controlled internally and which might be outsourced in some way. The traditional view has been to consider outsourcing specific functions such as office space planning and fit-out or facilities management functions. This could be described as vertical outsourcing where one or more functions are contracted out for part or the entire office portfolio.

The other situation which has emerged is where space is augmented by some or many features and / or services. A serviced office epitomises this situation where it likely[1] that a full package of space and service is acquired crossing the space / service boundaries and therefore might be described as horizontal outsourcing. This product can only therefore be compared to a more traditional property solution if the additional costs related to the infrastructure, service and management are built into the analysis. In order to do this occupiers would need good quality data related to each of the elements.

However, there is an increasing range of options available to an occupier. Figure 2 demonstrates that acquiring office space can range from purchasing a freehold where all the provision of infrastructure and management would be the responsibility of the occupier to using a serviced office where a complete package is offered. One of the key contentions of this research is that potential occupiers, when evaluating one extreme of this spectrum to the other in terms of total cost to the organisations, do not ensure that they are comparing like situations.

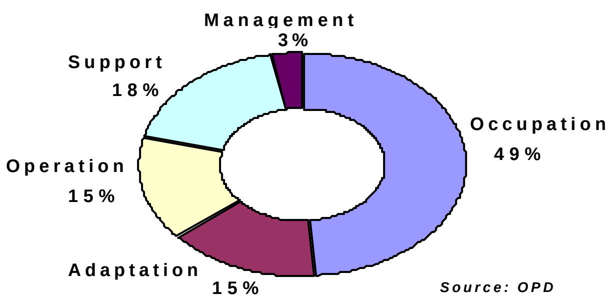
Figure 2: The Office Product - Service Continuum



Source: Gibson and Lizieri (forthcoming)

The importance of comparing Total Occupancy Costs (TOC) is highlighted by Figure 3. Although occupation costs (rent, rates) account for a significant proportion of the total cost, it is estimated that on average this may be only about half of the TOC. Adaptation (fit-out), running the office space and providing business support can account together for over 50% of the total occupancy cost.

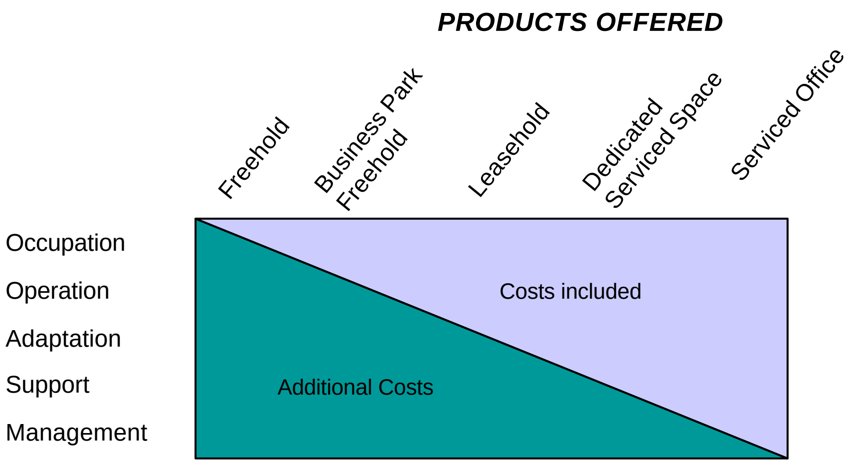
Figure 3: Estimated Breakdown of Average Total Occupancy Costs



[1] There are situations where serviced offices do not include the full range of FM or business support services and in some instances even the office furniture is excluded. This is particularly true of serviced office space catering for small organisations in secondary locations. See Gibson and Lizieri (1999) for more discussion of the structure of the serviced office market.

The cost perspective is highlighted further in Figure 4. This shows which costs are included in the "price" of the product offered and which are additional. Moving through the product-service continuum, a greater proportion of the total occupancy costs is included with the package. There is, therefore, a real danger of comparing the price per square foot or square metre of a standard lease with that of a serviced office. What is not transparent is that the first price excludes many of the costs that ultimately must be borne by the occupier, such as facilities management and reception, but which are included in the second. A further complication is that capital costs of equipment and furniture may not be fully taken into account when making the comparison. This may partially be the reason why some occupiers consider serviced offices to be an expensive option. The second reason is that, in the case of a serviced office, risks have been transferred from the occupier to the provider because of the short-term commitment to, and instant availability of, the space. Indeed most organisations ignore the hidden costs of inflexibility inherent in the structure of their property contracts that usually have a significantly longer time horizon when compared to their business outlook. It is this risk transfer element which is much more difficult to price.

Figure 4: Occupational Options and Costs Analysis



The overall dynamics of the relationship between the occupiers and the suppliers of space and services have become much more complex. There appears to be a wider range of new products and services being offered in the market place. Some relate to providing a bundle of services through a portfolio while others are linking the services to a specific property. If occupiers are to make sound procurement decisions about any of these new offerings then they need to have an explicit and rigorous framework for evaluating their choices.

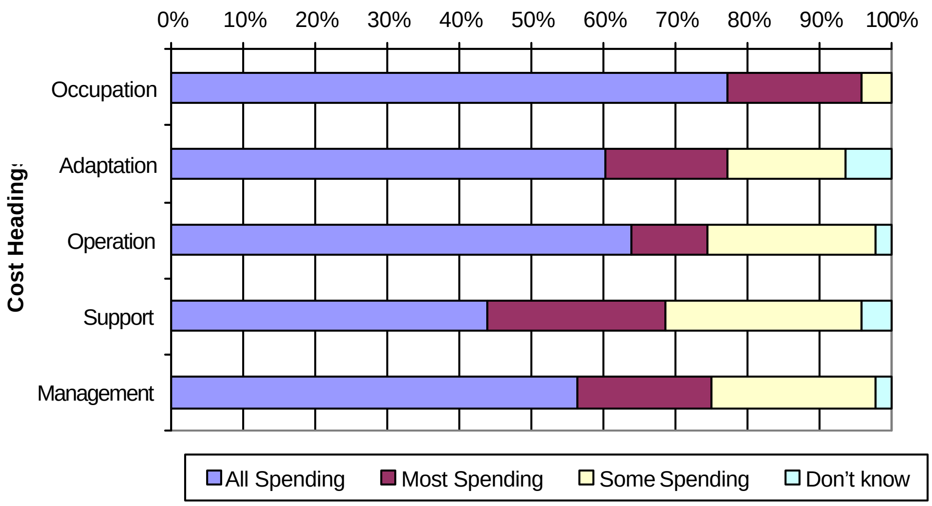
Occupancy Costs and Performance Measurement

When making a decision about a new requirement, property managers are likely to use their knowledge of their existing office portfolio to help inform that decision. This would be influenced by the available information on the cost of their current office space, how they evaluate an efficient building and the scope of their responsibility. Before corporate property mangers can evaluate their choices, and especially before they can start modelling alternative options with costed forecasts, they would need to have a good understanding of their own organisation's total occupancy cost base. This section considers the current data available within the respondents' organisations and the way that data is used. It also examines the role and responsibility of the different groups within each organisation in relation to the elements which make up a total working environment.

For the survey each respondent was provided with the total occupancy cost framework developed by IPD (see Appendix B). Costs are grouped into the broad categories of occupation, adaptation, building operation, business support and management. As shown in Figure 5, 96% of respondents claimed to have data related to the occupation costs for *all* or *most* of their occupied office portfolio while 69% claimed to have data related to the business support costs for *all* or *most* of their offices. These represent the best and the worst categories in terms of the likelihood of data being collected. However both these figures appear surprisingly high when compared to previous research which has investigated property data (see Gibson and Hedley 1999, Avis and Gibson 1995). For example, the most recent study found that over 60% of occupiers reckoned that they had insufficient information for some of their most important decisions including relocation, outsourcing, identifying under-utilised space, and sale and leaseback decisions (Gibson and Hedley 1999). This lack of data has often been highlighted as a constraining factor to better property management practice.

It is difficult to know if the current results represent a real improvement or just reflect the over-optimism of the respondents to this questionnaire. Regardless of the positive interpretation of these findings, at least a third of respondents still do not appear to have the data necessary to undertake an informed analysis of their total occupancy costs. This is borne out by responses to a series of statements in which just over 30% admitted that *"office costs, other than rent, rates and services charges were not collected and monitored centrally*" and that "*it was difficult to get an accurate picture of total occupancy costs as there were so many different departments involved in collecting the data*".

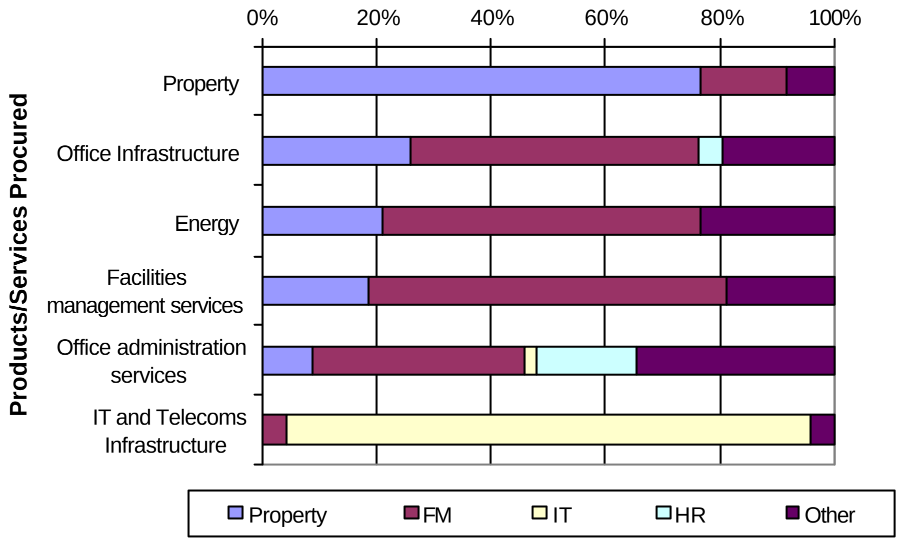
Figure 5: Proportion of Organisation's Collecting Data by Category



This latter statement substantiates one of the problems identified in the previous section. The way in which property products are being augmented with a range of services has lead to an offering which crosses organisational boundaries. Space, facilities management services and business support services grouped as one seamless product do not necessarily fall neatly into the remit of any one department. It is anticipated that property (space) acquisition may be dealt with by a department other than that which procures the facilities and / or business support services.

The survey again confirms this as shown in Figure 6. What is striking about this figure is the range of departments involved in the procurement of an operational workplace. The property department is most likely to be responsible for the procurement of space, the facilities management department with the procurement of office infrastructure, energy and FM services, and the IT department with the IT and telecoms infrastructure. The area most likely to be procured by different groups within different organisations is the office administration services. Not only does this split of responsibility highlight the need for good co-ordination in order to make sound workplace decisions, it also becomes difficult to identify which group should take the lead if an innovative product with extensive services is being considered. There is also the implication that it would be very difficult to broker outsourcing of space plus service. Consequently, the fragmentation of procurement leads not only to a potential lack of data, but also to a lack of clarity of responsibility and potential blockages in the decision-making process.

Figure 6: Departments Responsible for Procurement of Property, Infrastructure and Related Services



Having cost data is important but it is also necessary to have data related to the way in which office space is being used. The most likely information probably to be collected would relate to the size of the office. This is confirmed with almost 90% of respondents stating that they had data on the *net internal area occupied* for all or most of their office portfolio. This proportion fell to between 70% and 75% when considering the *number of workstations* or *staff based in an office*. Therefore, although the vast majority are able to examine costs on a square foot or metre basis, at least one quarter of the respondents would be unable to assess the cost per person or workstation for a significant proportion of their office portfolio. This finding is consistent with the Gibson and Hedley (1999) study that showed that access to IT and HR data was not available or only available with difficulty for about 70% of occupiers.

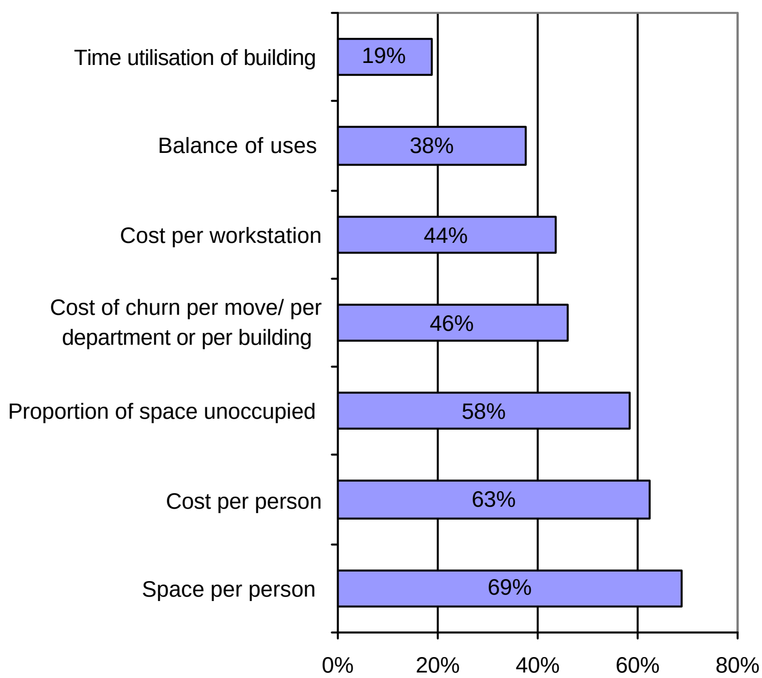
As well as having the data and therefore the ability to undertake this type of analysis, it is interesting to see which measures are actually being used to evaluate the efficiency of the current office portfolio. Efficiency should relate to how well the resources are being used by relating inputs (amount of space) to outputs. Examining the occupiers' views should provide some insight into what the organisation considers important in creating an efficient workplace.

Figure 7 shows the proportion of respondents using specific performance measures. In total, 80% of the respondents claimed to measure efficiency, which leaves one in five organisations using no such measures. This is considerably more than a recent survey on information and performance measures where only about half of the respondents claimed to have any measures of property performance (Gibson and Hedley 1999). Again this may reflect the over optimism of the group responding to this current survey.

Examining the measures used, space per person (69%) was used most often with cost per person following closely behind (63%) and then the proportion of unoccupied space (58%). Other measures included measuring the cost of churn (46%) and the balance of uses within the building (38%). Both these measures would be important when considering a generic office solution, possibly provided by a third party, as one of the drivers to using such space is the ability to move staff quickly and with minimal cost. It is difficult to tell if the cost per person measure includes any element related to churn. It may be that the cost of relocating staff within a building or between office locations is being ignored.

Similarly, finding the right balance between workstation areas and support areas including informal breakout space and meeting rooms has become an important aspect in gaining greater office efficiency, particularly if new working practices are being adopted. Finally the fact that less than 20% measure the amount of space temporarily vacant (or even the staff/workstation ratio) within a building suggests that there may be the tendency to focus on a static building with an emphasis on one desk for one person.

Figure 7: Proportion of Organisation's Using Office Efficiency Measures



Summary

The key findings in relation to occupancy cost data and performance measures which emerge from this section are:

- Although the majority of organisations participating in this research claim to have a wide range of data on office occupancy costs, there is still a significant minority which only track some of their spending. This is particularly the case in relation to the operation, business support and management costs of their office portfolio where as many as one in four only track some of the relevant costs.

- This lack of data may relate to the disjointed procurement of the individual elements which make up an operational office. In almost all cases responsibility for occupational costs was divided between at least two or three departments. The property, facilities management and IT departments were most likely to be involved.

- One in five organisations in the survey did not explicitly track the efficiency of their office portfolio. For those which did measure efficiency, space per person and cost per person were the measures most often used.

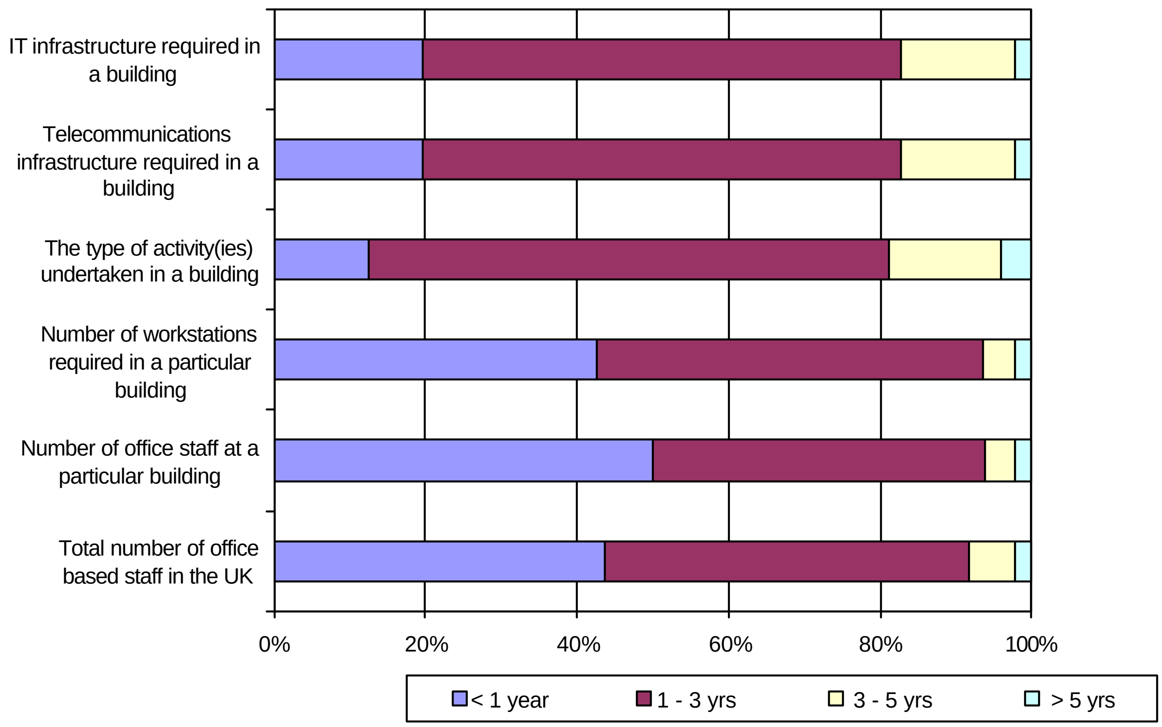
- The focus group will show that there are grounds for believing that occupiers can confuse the availability of data somewhere in their organisation with practical access to it for most decisions. It may be that the respondents are exaggerating the availability of data.

Assessing Future Requirements

The search for more flexible property solutions is driven partly by the increasing pace of change within organisations. In order to ascertain the pace of this change, respondents were asked to consider two aspects. First, how far ahead they were able, with reasonable accuracy, to forecast the key drivers of the demand for office space such as the number of staff and the IT infrastructure required? Second, respondents were asked to reflect on how much lead-time they had been given when asked to acquire new office space during the last three years.

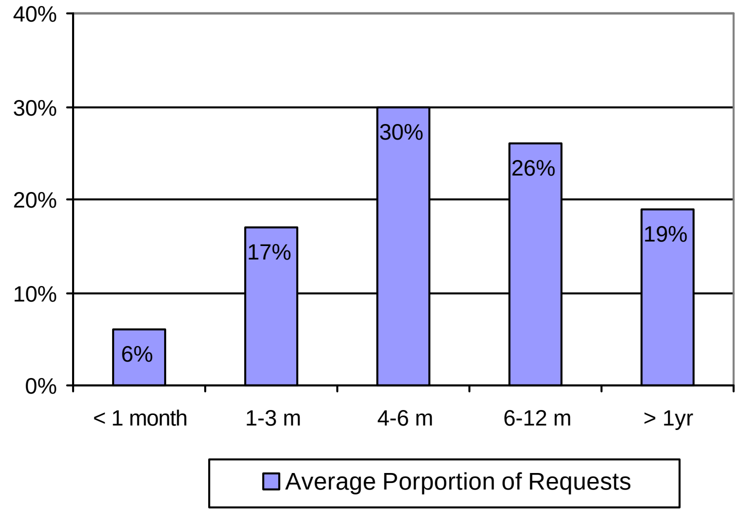
Figure 8 shows the results for the first aspect: the forecast period. It is often contended that organisations have difficulty in projecting more than one year ahead and certainly not more than three. This is fully supported by the results with less than 20% of the organisations claiming to be able to forecast any aspect more than three years. In fact between 40% and 50% of organisations would be unable to forecast the number of office staff in the UK, the number of office staff in a building or the number of workstations required in a building for more than one year. This clearly demonstrates that organisations consider that they are changing rapidly and are having to react to shorter product and business cycles, mergers and acquisitions, ecommerce and globalisation as well as wholesale corporate restructuring. It also ties in with the findings in the next section where 50% of organisations believe the ability to exit space is a very important criterion when selecting new office space.

Figure 8: Forecasting Period for Components of Office Space Demand



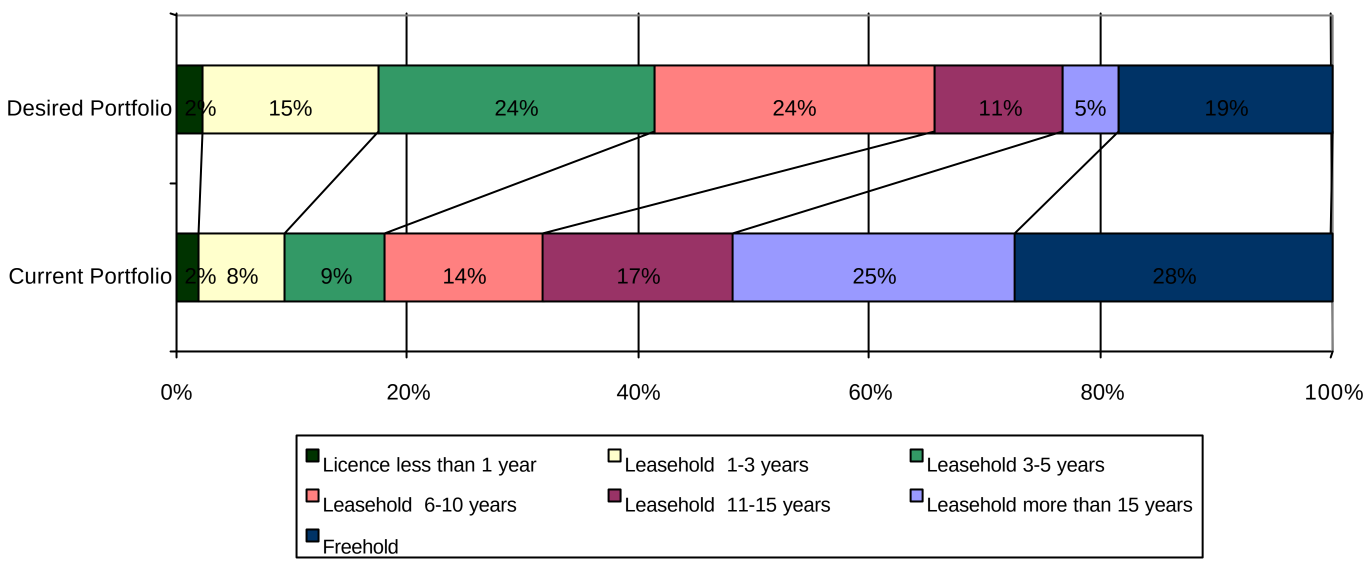
Examining the lead-time given on recent acquisitions, Figure 9 shows that in just over half of the cases less than six months was available to obtain an appropriate office property. This places considerable pressure on the property manager as there may be relatively little choice within the market during the acquisition period. To some degree this will depend on the criteria used to select office space, but from past research it is clear that often there are a limited number of options available in practice which meet the locational and space (volume) requirements at any point in time. Such pressure is typically exacerbated by the transactional and legal delays that property managers face in the UK. The heterogeneous and fixed nature of property, and the thin markets, mean that in contrast to all other factor inputs, it is virtually impossible to match requirement to product. Short lead-times and inflexibility on the supply side exacerbate this. Therefore it is not just the current portfolio that is mismatched to current needs, but also current needs are not matched by available product. This will be re-examined at the end of the section.

Figure 9: Average Proportion Requests by Lead-time Given



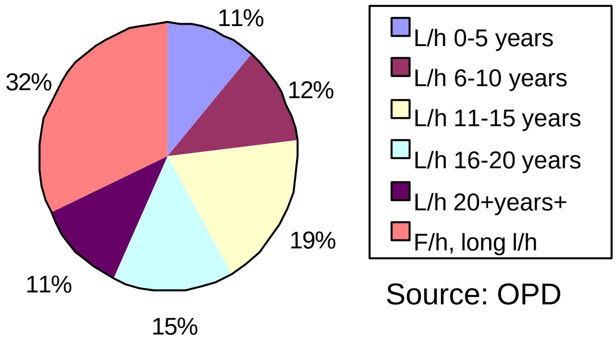
The problem of mismatch between an organisation's existing office portfolio and iits current needs particularly relates to the tenure and length of commitment. In order to gauge the degree of mismatch between what they currently occupy and what they would prefer to occupy, respondents were asked to estimate the proportion of office properties in a number of categories related to the tenure and length of contract. This is shown in Figure 10.

Figure 10: Average Proportion of Portfolio by Tenure and Length of Commitment: Current vs Desired



The bottom bar represents the average proportion of an office portfolio held in each of the different types of tenurial contract, from a license of less than one year on the left to freehold on the right. It clearly shows that, on average, more than half the existing portfolio is held either freehold or on a lease of more than 15 years. This finding is supported by OPD data in Figure 11, which shows that the proportion of space held freehold or under leases with a term of over 15 years, is almost 60% of total rental value. This focus on long-term commitment strongly contrasts with the planning period discussed above.

Figure 11: Office Tenure (end 1998)



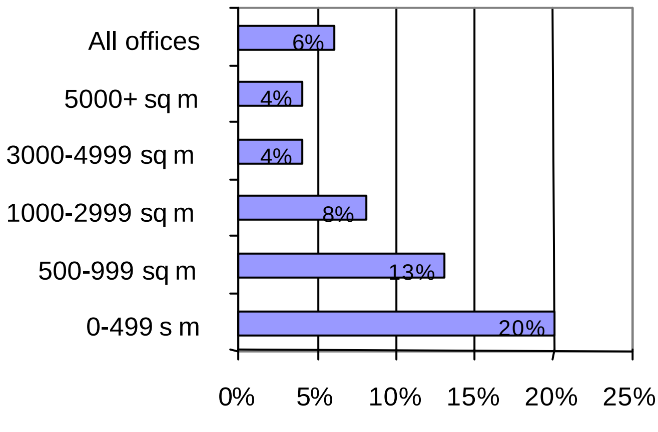
The top bar in Figure 10 shows the respondents' estimate of the terms on which they would secure their office space if it could be newly acquired today; in other words, their desired balance of tenure. The contrast between the current and the desired situation is clear. Starting with the longest contracts, the proportion held freehold or on a lease of more than 15 years, would fall from the current position of over half the portfolio to an ideal positions of less than a quarter. Of this a significant proportion would still be held freehold (19%), with the greatest reduction in leases of more than 15 years.

Although there would be an increase in the proportion of medium-term contracts, this is not as dramatic. The proportion of leases held on periods between 6 and 15 years would increase from the current position of 21% to an ideal of 35% of the total portfolio. The most significant increase in the proportion held would be in short term leases of between one and five years. The current proportion in this category was estimated to be 17% on average as where ideally it would be as much as 39% of the total portfolio. This finding reflects clearly the influence of shortening business cycles on organisations generally. What is slightly surprising, given that serviced offices were often considered for future requirements, is that the very short-term space, less than one year, was felt to be held in about the right proportion (2%). This may be because the respondents are looking at serviced office space not just on a very short-term basis but also for longer periods of up to say 3 years.

In the survey, there were some other interesting observations which could be drawn from the responses to this question. The shift towards shorter leases was clear with almost 60% of respondents stating that ideally they would not hold any lease of more than 10 years and almost 30% stated they did not want leases of more than 5 years in length. Of the third of organisations which stated that they would desire at least some of their offices held on a freehold basis, this was likely to be a significant proportion and in a few instances the entire portfolio.

This emphasis on freehold could well reflect the financial policy of the organisation or the view that real flexibility is only possible if there is total control of the asset and therefore can only be achieved through freehold ownership. Both of these factors have been identified in previous research (Avis and Gibson 1995). It is evident however that such attitudes may be partly a result of the high levels of vacancy to be found in office estates (see the OPD statistics in Figure 12). If there is on average a 6% vacancy rate in office space, some of the need for flexibility can be accommodated in the existing portfolio. This is not however supported by the respondents who agreed (75%) with the statement: "*Organisations can no longer justify holding surplus office space to cope with ad hoc short term requirements".*

Figure 12: OPD Vacancy Rates (end 1998)

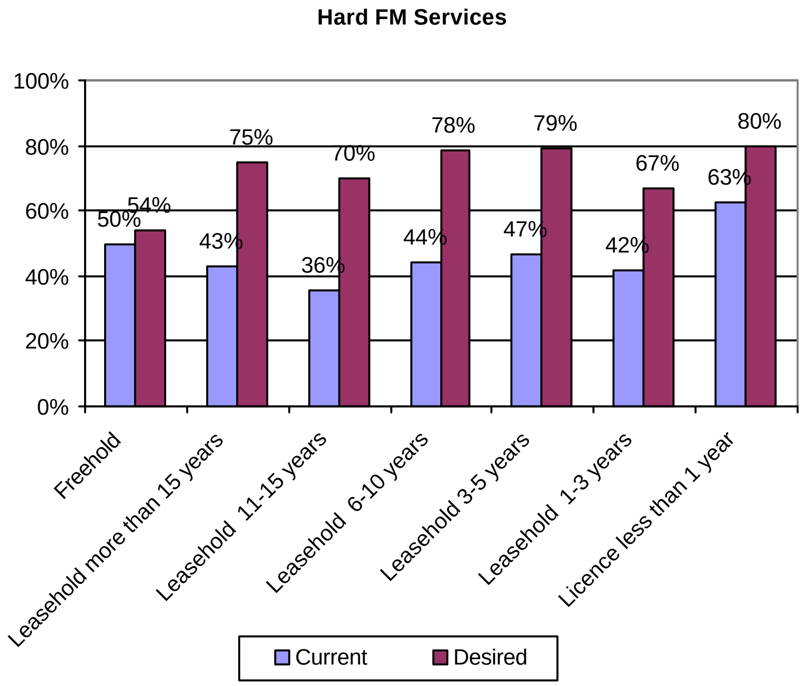


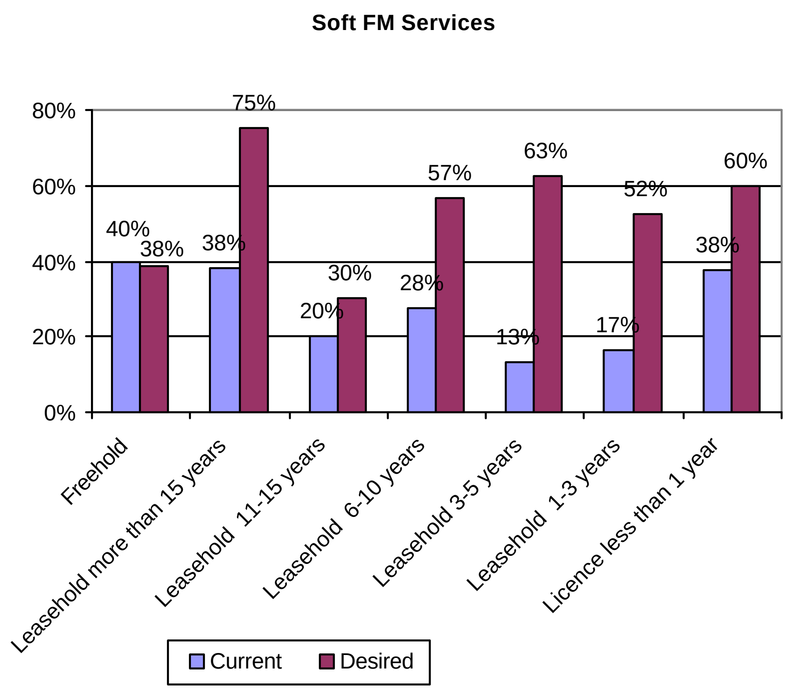
Source: OPD

The other aspect considered with regard to the current situation compared with the desired situation was the provision of services with the space. Figure 13 shows a comparison between the provision "hard" FM and "soft" FM[2] services related to each type of tenure choice. Although there appears to be some confusion about the interpretation of this question, with many stating that they had services delivered with all their existing property, the general trend is unambiguous. For all tenure types, there is a desire for additional services to be delivered. What is not apparent is if these services should be tied to the property and provided by the "landlord" or if they should be delivered by another party such as an outsourced FM contractor. As organisations are showing a migration to shorter contract periods, there is a possible requirement for more "packaged" office products. This need for more service is examined in the focus group review.

[2] Hard FM includes the maintenance, repair, cleaning, security of an office while Soft FM includes services such as reception, mail room, reprographics. These are equivalent to the Building Operation (type C) and Business Support (Type D) headings in the OPD Total Occupancy Cost Code (IPD, 1999).

Figure 13: Proportion of Respondents with FM Services by Tenure and Length of Commitment Current Provision vs Desired Provision





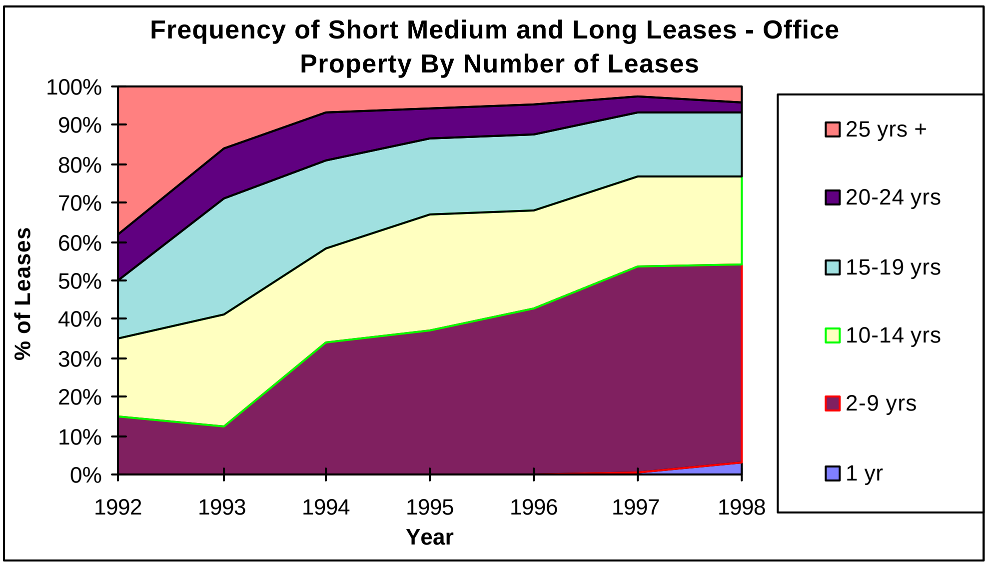
Given the desire for shorter tenure periods and the addition of more services, has the property market responded to occupiers needs? There is evidence that there has been a reduction in lease length where the average lease taken for all office tenancies has declined from over 15 years for leases starting between 1990 and 1993 to under 8 years for the period 1998 to 9. (Figure 14) This data is unweighted and therefore does not reflect the size or the value of the property and therefore masks a situation where large, well-located prime offices are still commanding long-term leases while smaller secondary units are available on much shorter terms. Nor does this reveal the diversity of terms in the market.

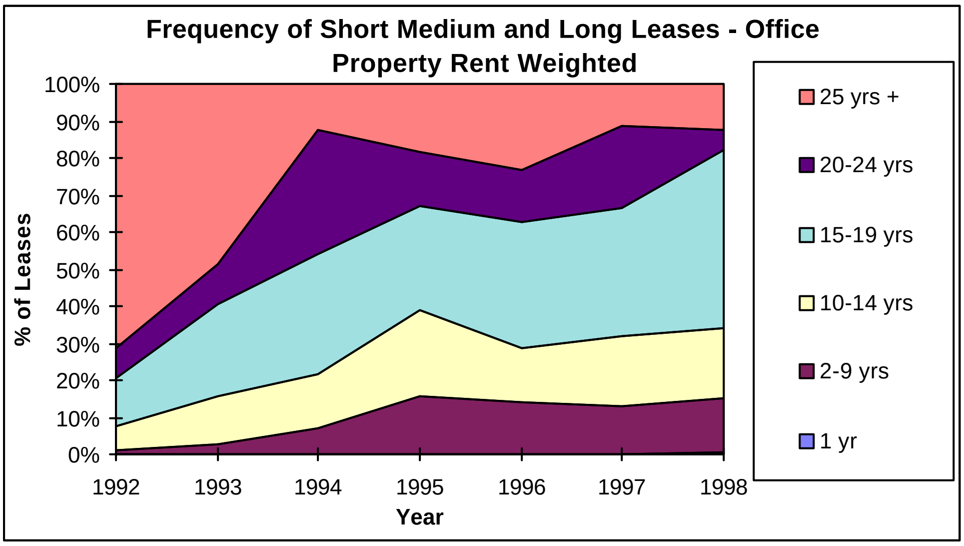
Figure 14: Average Term of Office Leases by Start Date

Source: IPD

Figure 15 again shows IPD data on offices but breaks down the length of leases into categories. As well as the decline in the 25-year lease, the most striking feature of these charts is the increasing spread of lease lengths. Additionally, the impact of rent weighting the leases as shown in the lower chart starts to uncover that, by value, the majority of new leases and renewals in 1998 were still more than 15 years in length in the almost two thirds of the cases. What is apparent therefore is that although the average lease length has fallen, there is a much greater diversity of lease lengths being offered in the market.

Figure 15: Lease Lengths: UK Offices





Source: Crosby et al 2000 from IPD data

The figures above appear to suggest that there has been a significant shift in the structure of the property market with no sign that the 20 to 25 year lease term has returned with the recovering lettings market over the last three to four years. However according to recent research (Crosby *et al* 2000) large lettings, regardless of location, tend to command longer lease lengths. On the other hand, there is also anecdotal evidence that there is hardening of the property market, at least in locations with high demand. In these situations, landlords again have the balance of power and therefore may be reverting towards a more traditional stance by offering only long term leases. The relationship between landlords and occupiers is again discussed in the review of the focus group meeting.

Summary

The key findings which emerge from this section are:

- As a result of business pressures, the forecasting horizon for most organisations is less than three years and in many instances is less than 1 year. The shorter horizons apply particularly to the total number of office staff in the UK, the number of staff at a particular office and the number of workstations required in a building. This demonstrates the highly dynamic nature of the demand for space within organisations today.

- The lead-times given to acquire new space are very often less than six months and almost always less than one year. The need for space to be operational quickly is apparent.

- The tenure and terms on which organisations' existing office portfolios are held are not consistent with their current planning horizons and need for flexibility. Ideally, organisations would prefer to hold their office property on much shorter leases with the majority not wanting a lease over 10 years. However it is also clear that they recognise that a balance of tenure and terms will best support their operational needs.

- There is a general requirement for increased provision of both "hard" and "soft" FM services although it is not clear who should be providing these services: the landlord or an external contractor.

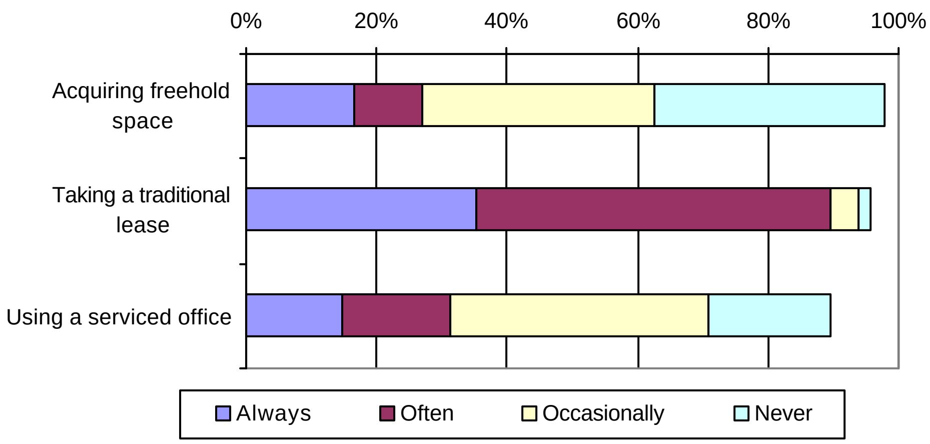
- There is a shortening and a greater diversity of lease lengths within the market. Evidence suggests that there has not been a return to the 20 to 25 year lease term despite the improved lettings market. However, by examining leases let during 1998, it is still clear that there is a divide between what occupiers really desire (leases of less than 10 years) and what the market is offering (15 plus years).

Selecting New Office Accommodation

There is evidence from the research that organisations require different office space solutions for different situations. The research investigated two aspects of how organisations evaluate the choices open to them. Initially the survey examined the types of property considered. How broad was the remit in terms of the range or products from freehold space to serviced offices? The second theme was the criteria used to evaluate the options. This latter aspect first considered a broad range of potential criteria from location to speed of occupation and then focussed particularly on the financial criteria. This was intended to draw a link between the initial investigation of total occupancy costs and the way occupancy decisions were made. Finally the type of financial analysis used to evaluate the acquisition of new property was examined to gauge the level of sophistication.

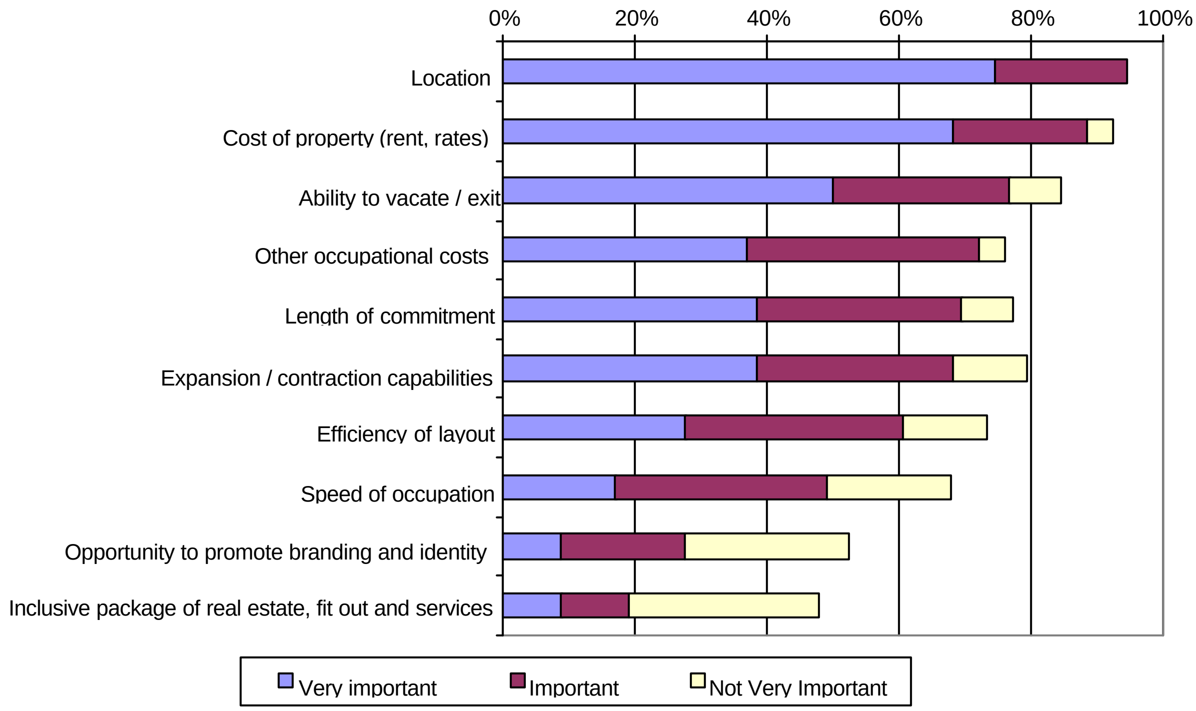
Examining the first aspect, Figure 16 shows that considering a traditional lease was by far the most likely with serviced space more likely to be considered than freehold. We also asked if they had changed the type of property they considered within the last three years. This was the case for just over a third of respondents with the key reason being related to the increasing importance of flexibility. The availability of serviced office space and the move to shorter leases were also mentioned as important drivers to change. Given this and the above analysis of the desired balance of tenure within a portfolio, it may be considered surprising that the traditional lease was so often considered. As outlined earlier however, previous research has highlighted that often occupiers are left with little choice as there are few office properties on the market at any one time which actually fulfil their requirement (Rowley *et al*, 1996). Of those that are available, the vast majority are likely to be on offer on a leasehold basis, with a "traditional" lease being the starting point. Additionally, if the shortening of lease lengths is genuine, then occupiers may be obtaining their flexibility through traditional leases with shorter terms. The split shown in this figure however might reflect the structure of the property market more than what the occupier would actually prefer.

Figure 16: Type of Property Solution Considered by Respondents



This hypothesis is further reinforced by Figure 17 which shows the criteria considered very important or important by the respondents. Location is the only criteria to be considered by all respondents as either very important (75%) or important (20%)[3]. This is closely followed by the cost of property with 88% rating it as important or very important. The third most important criterion was the ability to vacate/exit with 77% rating it as very important or important.

Figure 17: Criteria Used to Select New Office Space by Importance



Upon further examination of Figure 17, it is interesting to note that "*other occupational costs*" and "*efficiency of layout*" appear to be important but secondary criteria. This contrasts with the earlier findings on the review of cost data and performance measures, where both these issues are claimed to have some importance. Again this may be further evidence of the current inflexibility and inefficiency in the market which results in limited choice. Until, and if, property becomes a commodity which can be purchased at a price, the dynamics of location, at least in a micro-sense, will continue to be the key determinant of choice.

We also asked respondents to consider what financial criteria they would use to evaluate a choice between more than one appropriate office (Figure 18). Rental cost per square foot / metre was mentioned most often: by more than 90% of the respondents. This seems to reflect the tendency to focus on direct property costs alone without due regard for the amortised fit-out and infrastructure costs or the running costs, although they might be judging that such costs would be similar for all potential buildings.

However over 80% claimed to consider the running cost of the building (85%); the cost of fit out (85%) and the total occupancy cost (83%). This last figure must be drawn into question as only 47% claim to consider the cost of office furniture and 32% the cost of office administration. However these are defined, if total occupancy cost is to be taken into account, these costs must be built into the equation. This continues to highlight the difference between organisations' understanding of the term "total occupancy cost" and the way in which they use this data. Concern continues to be expressed that organisations are comparing "apples with oranges". If a total office solution, such as a serviced office, is being considered,

[3] The remaining 5 % did not respond to this question.

then there needs to be a mechanism to ensure that the costs being compared are equivalent. This means that costs need to be considered, not only in terms of space and square footage, but also in terms of the total service package included in the offering. At present it appears that few organisations are able to do this analysis.

Figure 18: Financial Factors Considered when Selecting New Offices

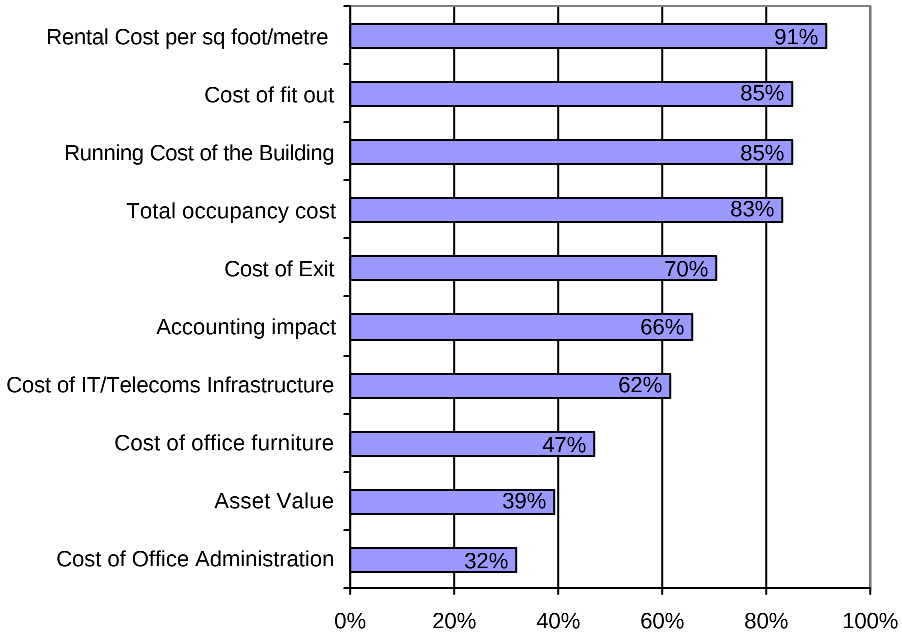
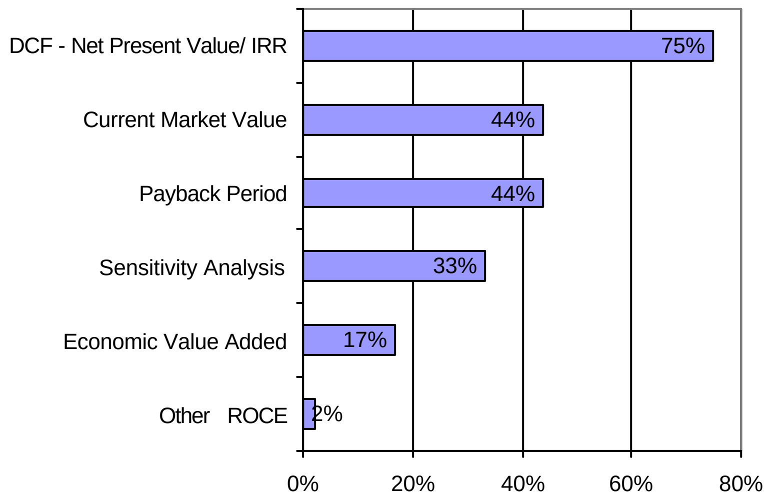


Figure 19: Financial Analysis Undertaken



Following this one step further, the financial analysis used when selecting new office accommodation appears, in the main, to be based on a Discounted Cash Flow (DCF) analysis with Net Present Value (NPV) or Internal Rate of Return (IRR) as the final criteria. Almost three-quarters of respondents stated that they use this method (Figure 19). Although this is laudable, and a vast improvement on the more traditional property analysis, there appears to be limited awareness of the usefulness or insight to be gained from this technique. Only one-third claimed that they used sensitivity analysis in their evaluation. If this figure is correct, given the uncertainty unveiled in the section on forecasts and lead-times, it is worrying that different business assumptions of the future are not routinely tested. An early exit, an unanticipated expansion or an extension to a project could have a highly significant impact on the final value of any proposed solution. This type of testing may be being undertaken but in an unsystematic way. However, given that the aim of sensitivity analysis is to determine how vulnerable or robust any option might be to these sorts of changes, it is the key to evaluating the risks associated with any one option and therefore should be explicit.

Summary

The key findings related to the selection of new office accommodation are:

- That, despite the desire to hold shorter leases, the type of property most often considered when looking for new accommodation was a traditional lease. The conclusion may be that this is what the market has on offer rather than what the occupier really would prefer.

- In terms of general criteria used to select new office space location, cost of property and ability to vacate or exit are the three ranked as very important by at least half the organisations. Again this reinforces the short planning horizons and lack of certainty about the future. Although other occupational costs are considered important, it is interesting that the greatest focus is still on the direct property costs of rent, rates, etc.

- This emphasis is confirmed by the costs considered when selecting an office. Rent, the running cost of the building and the fit-out costs are looked at most often. Although over 80% claim to consider the total occupancy costs, less than half take into account the cost of furniture and less than a third the cost of office administration. Unless these non-property costs are considered similar in all buildings/locations, there continues to be a lack of understanding about which costs should be included in a total occupancy cost calculation.

- Although organisations appear to be using some form of DCF to compare their options of new office space, only a third are using sensitivity analysis. If true, this is surprising, given that the forecasting horizons are so short and that the ability to vacate was a very important criterion. Without this analysis the risks associated with any one option cannot be ascertained.

Reflecting the Views of Participants

The three previous sections reported on the key findings from the survey related to organisations' practice. This data needs to be balanced by opinion in order to gain a clearer understanding about what this information is telling us. There were two ways in which opinion was sought in this research. First, within the survey there were a number of statements with which respondents were asked to either agree or disagree. These were developed in order to obtain a broader perspective on the issues addressed by the survey. Secondly, a focus group was held in early January where the initial results of the survey were discussed. There were six external participants drawn from the respondents to the survey plus four members of the research team who took part. The external participants represented organisations in a range of sectors including IT, financial services and local government. This section of the paper will report on both of the opinion-gathering elements of the research.

Survey Respondents' Opinions

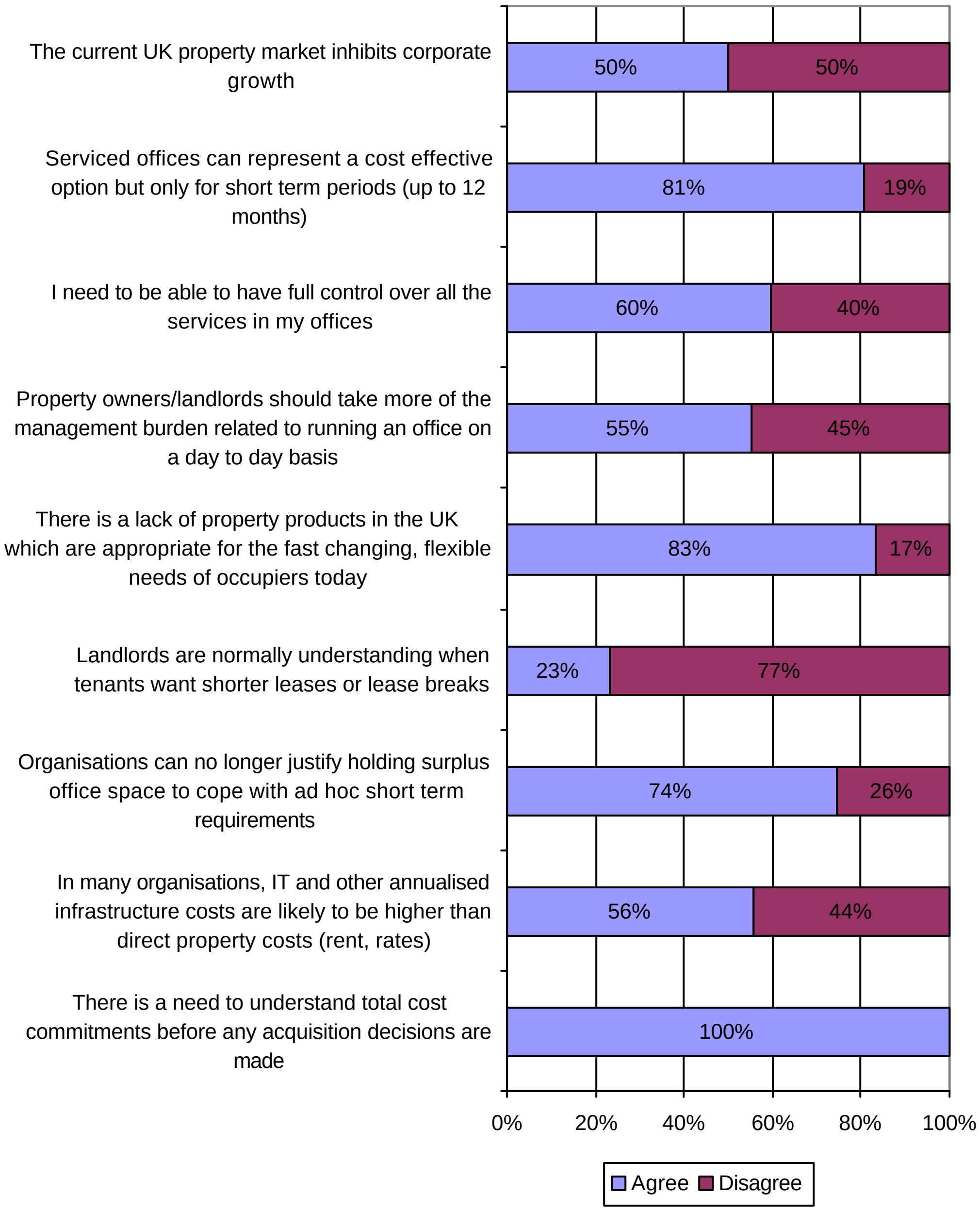
The series of statements which respondents were asked to consider are given in Figure 20. These statements can be group together into the three themes: property market inertia, service requirements, and cost issues.

There appears to be a lack of agreement as to whether the property market acts as an inertial force. Half of the respondents agreed that "*the current UK property market inhibits corporate growth*" while the other half disagreed. However there was more consensus when asked about the relationship with landlords and the products on offer. Just over three-quarters disagreed with the statement "*landlords are normally understanding when tenants want shorter leases or break clauses*". Similarly over 80% felt that there was "*a lack of property products in the UK which are appropriate for the fast changing flexible needs of occupiers today*". Both of these latter statements appear to support a view that occupier needs and wants are not currently being met by the property market. The reason why many respondents may not feel that the UK property market inhibits *corporate growth* is that the bigger issue for organisations has been *corporate change* not necessarily related to growth. This was apparent in the general comments made by survey participants who often spoke of the changes their organisations had recently been through including major corporate restructuring, mergers and take-overs, and changing organisational status.

In terms of service requirements, it appears that the respondents were split over who should be providing these services. Just over half (55%) agreed that "*property owners/landlords should take more of the management burden related to running an office on a day-to-day basis*". However 60% of respondents felt they "*needed to be able to have full control over all the services in their offices*". This second statement may appear inconsistent with the desire for landlords to take more of the burden. The word control here may be being used not to mean responsibility for the services but the ability to define requirements explicitly. This will be considered later where focus group participants stressed the need for well-defined service level agreements (SLAs) when outsourcing service provision to any third party.

Finally, understanding cost was seen to be essential by all the participants who agreed with the statement "*there is a need to understand total cost commitments before any acquisition decisions are made*". Four out of five respondents also agreed that "*serviced offices can represent an effective option but only for short term periods (up to 12 months)*". It also appears that at least some organisations (56%) feel that "*IT and other annualised infrastructure costs are likely to be higher than direct property costs (rent, rates)*". Together these point to an understanding of the changing cost dynamics related to occupying business space. The second statement appears to highlight the cost associated with flexibility, particularly related to very short term requirements, while the third demonstrates the changing balance within the cost structure when creating a workplace.

Figure 20: Analysis of Statements on Suppliers, Occupiers and Property Market



Overall, the opinions gathered from the respondents seemed to confirm the perception of a changing marketplace. Although they did not conclusively state that the property market acted as an inertial force, there appeared to be a frustration with the existing relationship with their landlords. There was also a dilemma concerning the provision of property-related services: a tension between more support from the landlord and the need for control. Finally they recognised the importance of fully understanding total occupancy costs and appeared to acknowledge that the occupancy cost profile was changing.

Focus Group

The focus group considered the key findings which emerged from the survey. The discussion was wide-ranging and allowed all participants to engage in the debate. In reflecting on the comments they can be divided into five themes:

- the importance of total occupancy costs;
- where and how business decision were made;
- evaluating property choices:
- business change and time horizons;
- occupiers' needs and wants

This section will consider each of these themes in turn.

The importance of total occupancy costs

"*What we like to think we know, what we actually know and what we want to know are very differen*t."

This quote summed up the view of the participants concerning the data organisations have on total occupancy costs. The key point was that the senior manager responsible for corporate property (the respondent to the survey in most instances) often had an inflated view of the cost data that was available. This was reinforced by a comment that "*the information is available – somewhere - because we paid for it but that data is often not accessible – even in the medium term*".

This lack of availability of data was debated at some length. The participants agreed that often the data is split between different decision-makers or departments. Often the only place where all the information required to calculate total occupancy cost was at a high level where there was probably only marginal interest in the issue. There was also the problem of the division between those who use (occupy) the space and those who pay for it, making it difficult to assess the cost effectiveness of any particular office. Overall there was agreement that, although much of the data may exist, at present there were few organisations who could access it readily and report the information to an appropriate level.

There was some debate about costs associated with capital expenditure including freehold property. If these were to be annualised, choosing the appropriate life of the asset as well as the appropriate cost of capital or interest rate was difficult. Each organisation appeared to have developed its own approach but a common theme was the difficulty in building these types of costs into a decision-making framework. As one participant stated: "*Interest comes in as an overhead but is not seen by the user. This distorts decision-making; freeholds are seen as cheap*". Again this highlights that data needs to reach the appropriate decision-maker in an organisation if rational decisions are to be taken.

Another theme of the cost debate was the importance to collecting total occupancy costs regardless of how difficult it was. On the one hand it was agreed that the occupation costs needed to be put into context either in terms of the total operational costs or the revenue stream and that this would demonstrate the relative importance of these costs for each organisation. On the other hand there was a divergence of view as to the importance of these costs. There were examples given where the business need (and potential revenue) far outweighed any concerns about property costs encapsulated by the view "*The first driver for property is business support*". There were also examples where the importance of raising the understanding of property costs across the organisations was paramount particularly as organisations attempt to change culture. '*We moved from a culture where everything (property related) was free to a business unit focus, where each business unit manager has full cost responsibility. We had to educate them in the "true cost" of running the business*". What appears to emerge is a recognition that occupation costs are likely to be taken into consideration in different organisations at different times. This will depend on factors including the industry sector, the relative impact of property on the business, the lifecycle of the company and particular moments of business change which bring property to the fore such as downsizing, restructuring or culture change.

Finally, there was a view that property cost information systems, although still not ideal, had improved significantly within the last five years. Not only did the property data need to be made more available, it also had to be "quality data". As one participant observed: "*This is where we are say 80% there – is that good enough? What we need to look for is continuous improvement*." There was a call for a clearer definition of costs to be accepted in order that benchmarking and a better understanding of the dynamics of occupancy costs could develop.

Overall the debate on total occupancy costs revealed that generally organisations have the data but it is often inaccessible and may lack quality. TOC was felt to be more important in some organisations than in others and this would depend on a range of circumstances both external and internal to the organisation but that, in order to raise the profile and understanding of the property resource within the organisation, the ability to benchmark costs externally was fundamental.

Where and how business decision are made

"*Corporate politics and organisational structure make decision-making diffuse.*
Power can change day-to-day."

The way property decisions are made is probably no different from other types of organisational decisions. The group agreed that although there was an attempt to take rational property decisions, that judgement was often overturned by corporate pressures. The examples given ranged *from "we have the money*" to "*I don't care if the building is only required for seven years, look at the revenue that will be generated*." From a true business perspective these may be rational decisions and they highlight the conflicts many corporate property managers encounter.

There was also concern about the short-termism of corporate managers. Decision were often made by looking at the impact of a decision on the Profit and Loss account for only the next quarter, half-year or year. This was highlighted by one participant who said: "*They want a new building but only focus on 1 years rent or 1/40th of the capital cost. They lack an understanding of the risk exposure*."

The other concern was about accountability. In different organisational structures it was often difficult to determine where responsibility lay. For instance in one organisation the products were managed globally yet the costs were managed geographically. There were lots of individuals who had a stake in the property decisions and associated costs but no one group who carried the responsibility for all of these, except for the property group and only in an indirect way. An additional complication was that business managers changed role every two or three years and therefore left the legacy of their property decisions to the next incumbent.

This organisational structure issue was clearly related to the problem of data availability. The structure determined the accounting framework which in turn determined the way data was analysed and reported. In the example above revenues were reported by product line while costs were reported by location. Additionally it was acknowledged that different managers were likely to have responsibility for specific aspects of the workplace and report through different lines. Again it was highlighted that at the level at which these costs finally came together, the individual responsible was not likely to be very interested.

A final comment concerned the type of incentives used to motivate individuals within an organisation. The example given was that sales teams are usually given revenue targets rather than profit. If decisions were made which enhanced the revenue but ignored the costs then non-optimal property decisions were likely.

Evaluating property choices

"Flexibility has no value unless you want it"

The focus group broadly agreed with the criteria used to select new office accommodation as identified by the survey. However they did comment on a number of issues. First, location was seen as "*too woolly a term*". Location will mean very different things depending on the perspective and circumstances. It could relate to access to staff, clients or the quality of location in terms of resale or re-let. They felt that to really understand the issue, the variety of components needed to be unbundled.

Secondly, using flexibility as a criterion was also seen as a problem. As the quote at the start indicates, having flexibility is only appropriate if it is required. One participant was adamant that the flexibility should only be paid for when the option was exercised. For instance if a break is negotiated, the cost of the break should not be built into the rent but rather there should be a penalty for exercising such as 2 years rent. This is but one occupier's view. While some of the other participants indicated that they had negotiated similar terms, other remained silent. This highlights one of the major problems in the property sector: how to develop and price a contract with options of flexibility. At present it appears to be rather ad hoc with each landlord and occupier agreeing terms as necessary but not really understanding the property market reaction to this in terms of property value.

The other key theme to this part of the discussion was how decisions on new office accommodation were made. This was described as an iterative process, often originated by a business unit which might indicate it needed a new office in a particular location. The corporate property team might examine this request and find that some of the staff may be better (more economically) housed in alternative accommodation. This is then suggested to the business unit which adds other dimensions to the request and so on. Through this process it is often difficult to identify any of the criteria used explicitly as they have evolved throughout the process.

The other aspect was that once the general criteria have been identified, there often is little if any choice within the property market at any time confirming the earlier conclusion. "*None of the buildings available is ever perfect*". Not only that, often the deciding factor is very subjective: the look or feel of the building, proximity to senior manager's home, golf club were all mentioned as the ultimate deciding factor.

This lead to a discussion of who had the ultimate power in any property decision. There was considerable variation from one instance where property was seen as a corporate resource and allocated centrally with the little input from the business unit manager to another situation where the business unit manager had the final say as they were the one to sign off the business case. In this instance the business unit manager is all-powerful.

Business change and time horizons

"*The move to shorter time horizons is evident but that hides the diversity. Some parts of the business are easier to plan and forecast than others."*

There was general agreement that time horizons were shortening but this varied both between and within companies. The point was made that North American and UK-based companies were driven by the associated capital markets where the performance of equities was tracked on a quarterly basis. The individual company therefore had to conform to the importance of short-term measures of performance. On the other hand German and other Northern European companies have traditionally relied on a greater proportion of debt financing and their capital market appears to be structured around longer-term returns. This therefore allows the organisation to adopt longer-term planning horizons. Given than all the participants, bar one, worked for UK or US based organisations, it is difficult to tell if this is a genuine perception or a case of "*the grass being greener on the other side*".

The second aspect was more directly related to the quote. Even within companies there are some part of the business which are easier to predict than others resulting in a split between a core and periphery requirement[4]. Another analogy was used which described organisations as *'lava lamps with some parts of the business ascending and others falling. Each takes its property with them and that is when the adjustment is necessary. This is often hard to predict.*" Looking at the issue of time horizons appears to be more varied than one might first anticipate.

Another perspective on business change related to how that change actually takes place. It was noted that in reality companies cannot grow organically that quickly and therefore are probably not taking on significant amounts of new space. However it was also noted that growth through merger was increasingly the norm and that this approach created a range of other problems and could fundamentally and quickly change any well laid plans.

Finally, there was some debate about the impact of ecommerce and the development of companies within that sector. It was felt that here the pace of change was highly dynamic and that the typical lifecycle of an organisation in this sector was very short when compared to the current norm. This was felt to have an impact on shortening the lifecycle of many if not all companies and the wider impact of e-commerce was felt.

Occupiers' needs and wants

> *"I want it [space] today but if I don't want it tomorrow, next month, next year then I want to get out!"*

The shift to short-term requirements was confirmed and reinforced by the focus group. The quote above articulates the ultimate desire of one of the participants. This desire to be able to terminate a contract, albeit with a pre-agreed penalty, was widely accepted as a better solution. Their current position was that freehold was still seen as the only option where they could gain this flexibility. "*If I don't need the building I can shut it down and reduce the running costs to a minimum*".

There was considerable debate over the way services were delivered and the way in which they might be delivered in the future. The participants stated that most of the hard FM and at least some of the soft FM were already outsourced and therefore there was little concern whether a property owner / landlord or another outside contractor provided these services. The important point from the participants' point of view was ensuring that the appropriate level and quality of service was being delivered and that over time they built a relationship with the provider. *"The key is having a tightly drafted SLA (service level agreement) with a provider I can trust."* It remains to be seen whether outsourced contractors or serviced offices can better provide this level of reassurance.

When asked about their experience of services being delivered with the property, the discussion initially focused on the serviced office market. Most used, or would like to use, serviced offices but felt the market was not mature enough and therefore the costs were too high. As one participant said: *"We already run internal serviced offices for our organisation and we can do it a lot cheaper"*. Others felt that the serviced office solution was particularly appropriate for small numbers of staff. *'If we need space for up to 30 staff it is uneconomic for meeting rooms, conference rooms and receptionists to be provided by us…Serviced office providers should be able to do t cheaper."* There were two areas mentioned as potentially creating difficulty in a serviced office environment: branding / identity, and the reception where

[4] Corporate property portfolios can be divided into core and periphery space. The core space would be held long-term but the organisation would need functional flexibility to alter it to the current business needs. The periphery space would be shorter term with financial flexibility being most important. See Gibson and Lizieri (1999) for more discussion of this model.

customers were greeted. The need to have more control over these was felt to be important but when probed it was dependent on the activity being undertaken in those spaces.

Ultimately, many of the participants were interested in "private sector PFI" contracts where the whole portfolio was handed over to a third party, although there was real concern over the extent of the commitments required. They did not feel threatened by this but saw how some property managers might. Their view was that their role would become more strategic, managing the outsourced contractor and liasing with the business in terms of its property needs. They could then focus on the real issue of how better to support the business and add value.

Summary

The key findings for the qualitative analysis are:

- The supposition that the survey results on total occupancy cost data were optimistic was confirmed by the focus group. The inaccessibility of the data was highlighted as the real problem and was due to a wide range of organisational constraints from fragmentation of property-related activities to overall organisational structure. However there was a general belief that understanding total occupancy cost was important, not only for decision-making about future requirements, but also to gain a greater understanding of property performance through benchmarking.

- Property decisions were felt to be driven by the same corporate pressures as any other decision. Politics, short-termism, internal performance measures and lack of accountability all influenced the final decision. Understanding this wider context was seen as key to influencing and working within the corporate process.

- Although the criteria used to select new office space cited in the survey were appropriate, the way they were used in practice was often through an iterative process and therefore difficult to pinpoint in practice. Additionally, the actual choice available was often limited and therefore organisations were often making compromises in their final decision. The degree to which the property group had the ultimate decision-making power also varied between organisations and this had significant implications for the final criteria used.

- Although time horizons were in general getting shorter, there were some parts of the business which were easier to forecast than others. This diversity lead to the split between core and periphery requirements. The greatest change was not likely to occur through organic growth but as a result of a major organisational change such as a reorganisation or a merger. These were the circumstances which were much more difficult to predict.

- Flexibility was very important to occupiers, particularly the ability to exit quickly. The way in which the UK property market was structured created significant problems due to the inherent inflexibility in the lease structure and the difficulty in pricing any flexibility which might be negotiated. Although serviced offices met this requirement for flexibility, the lack of market maturity and a perception of high cost was inhibiting organisations from adopting this as a broader solution.

- Outsourcing both hard and soft FM was fully accepted and already in place in many organisations. The important issue was not whether a property owner or a FM contractor was best placed to provide these services but rather the need to develop clear, well-defined service level agreements.

- For some occupiers with high salary costs, marginal differences in fit-out, operational and business support costs are inconsequential. As a result they are not significant factors in the decision-making process.

Conclusions

The demand for and supply of office property in the UK has changed significantly in the last decade. Occupiers want greater flexibility in their accommodation and increasingly recognise the need for good quality support services to make a building both efficient and effective. The property market has responded by developing some innovative products which seek to bundle the space with services. At the same time a wide range of new service providers have also emerged to offer packages of service to occupiers on a contract basis.

This diversity has created challenges for corporate property managers. How do they decide which are the most appropriate property and service solutions for their own organisation's requirements? In order to evaluate their alternatives they will require both data and a clear decision-making framework. The aim of this study has been to examine the extent to which corporate property managers are in a position to make informed choices.

There appears to be a continuing problem of data availability. Although many of the survey respondents claimed to have much of the cost data required to calculate the total occupancy cost of a particular building, the underlying problem appears to be the lack of access to that data at the appropriate level or at the appropriate time. The organisational structure, internal accounting regimes and fragmentation of responsibility were all issues which undermined the ability to gather together the required information.

Corporate property managers recognised the importance of having this data on two accounts. First, in order clearly to demonstrate the relevance of property decisions, past and current, they needed to be able to evaluate their cost property base both relative to their own internal operational costs or revenue and ideally to be able to benchmark these externally with similar office users. Secondly, when looking at various new property offerings, they needed to have a context within which to evaluate these choices to allow for modelling, evaluation and forecasting.

The lack of access to data was frustrating but a weakness that many corporate property managers were attempting to rectify, though in an incremental way. The acceptance of an industry-wide definition of occupation costs was seen as fundamental to taking this forward.

When assessing future requirements, it was clear that forecasting periods were very short relative to the way the property market was structured. The forecasting horizon for most organisations was less than three years and in many instances less than one year. However the focus group found that there was great diversity within any one organisation with some activities being significantly longer-term than others. This supported the idea of having core and periphery property requirements: the core supported by long-term property with the periphery supported by shorter-term commitments.

This drive to shorter-term commitments meant that the way many organisations currently held their corporate property was unsuited to the current situation they now found themselves in. Almost 60% of the respondents did not want any lease over 10 years. There was evidence that the property market had responded in part to the aspiration for shorter leases but not to the extent occupiers currently desired with lease lengths of 15 years or more still being the norm, especially for larger lettings. During discussion, the focus group highlighted the ability to exit as being a more important factor. Although shorter contracts were an issue, even more significant was the ability to walk away when a property was no longer needed and to stay if it continued to be required.

The need for more services to support the office was clearly evident with respondents desiring more services for all types of property contract. Whether the services were provided by a space provider (landlord / developer) or external contractor seemed unimportant. Ensuring that the services were delivered at the appropriate level of quality and in a timely and consistent manner was of much greater concern. The development of well-constructed service level agreements and the ability to exercise control appeared to be the way forward for many corporate property departments. This approach may be fine for major occupiers, but a small or medium sized organisation may not have the resources to negotiate or monitor a satisfactory arrangement.

The way new office requirements were evaluated reflected the growing importance of flexibility. The top three criteria identified in the survey were location, property costs and ability to exit. These were confirmed and supported by the focus group. However there were observations that property decision-making was often not clear-cut. For instance, the business unit mangers who required the space were often unclear about their own requirements, or the ultimate decision-maker, possibly the business unit manager, did not use any of the so called important criteria in the final selection. Additionally, choice in the market was often limited to making compromises and trade-offs necessary. All of these undermine the ability of any one individual to make an informed property decision.

The degree to which organisations understood the financial risks associated with their property decisions was difficult to ascertain. The survey showed less than a third of respondents stating they use sensitivity analysis yet the focus group stated that this financial investigation was part of the iterative decision-making process. However, the focus group also remonstrated about the short-termism in decision-making and a tendency not to look at the full costs over the life of the building or contract. Overall therefore, there does appear to be the potential for ignorance of the risks involved in property decision-making.

Finally, the new products within the property market, such as serviced offices, were accepted and broadly welcomed. The vast majority of respondents to the survey claimed to consider a serviced office solution at least occasionally. From evidence at the focus group this depended on the activity and number of staff requiring office space with it being seen as most appropriate for small groups, less than 30, who would have little contact with clients on site. However, there was concern that these products were expensive and some felt they could provide the same quality of environment and service more cheaply in-house. With greater transparency of the cost structure by the serviced office providers, the focus group felt that this sub-market would gain increasing acceptability.

The research had uncovered a number of forces of resistance within occupiers to the changes in the market. The lack of available occupancy cost data within many occupiers undermines their ability not only to fully evaluate new requirements but also to assess their current performance. The fragmented way corporate property is often managed makes if difficult to identify and co-ordinate activities, and to compare these to new property products on offer in the market. The short-termism within organisations leads to a tendency to focus only on annual costs and often over a short period distorting the risk exposure of any decision. It is this organisational context which makes it difficult for corporate property managers to develop a clear and rational framework for decision-making.

There is a desire and will to change things on the part of corporate occupiers. Property cost information is continuously improving. Occupiers want to gain a better understanding of the benefits of these new property packages but they also need a much clearer understanding of the costs. They want greater flexibility and are willing to pay but there is still a need to convince both providers and occupiers of the value (price) of transferring risk.

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A: Corporate Occupiers Survey: Evaluating office Space Needs & Choices

B: Total Occupancy Cost Code (TOCC)

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