Portfolio optimization: The right size at the right time

Modeling supply against demand can help real estate stay ahead of the curve and better support business objectives.
Over the last five years businesses have not been completely static. The global economy has been chaotic and the effects have created ongoing volatility in many organizations. The upheaval is reflected directly in the ever-changing C-Suite mandates that Corporate Real Estate (CRE) organizations must meet. This year’s, “reduce overall space footprint,” might be next year’s “support business growth of 20%.” Mergers and acquisitions, divestitures and downsizings often loom on the horizon. How can a CRE executive stay ahead of these demands and proactively support business needs?

One effective tool for CREs is to match the organization’s portfolio to its changing business goals through portfolio optimization. Quite simply, portfolio optimization is a comprehensive process that models real estate supply against real estate demand to drive efficiencies across a portfolio.

Why portfolio optimization?
The most compelling reason to optimize the portfolio is also the most persuasive to business leaders: it saves money. Portfolio optimization eliminates wasted space, which translates directly to lowering the cost of real estate, typically the second or third largest item in a corporate budget. A comprehensive optimization program can reduce space needs by up to 2%, saving as much as $1,000,000 in annual run rate in a 3,000,000 square foot portfolio.

However, portfolio optimization is not always specifically about downsizing a portfolio, but rather right sizing it for business objectives of any given time. Sometimes the goal may be focused on reducing the overall footprint, but if an organization delivers a top-down objective of growing markets by 20%, it’s possible that more, not less, space will be required. Portfolio optimization helps provide the right space at the right time to serve a company’s ever-changing and ongoing needs. It aligns with not only business objectives from “normal” expansions and contractions, but events such as mergers/acquisitions and divestitures, and often includes changing processes such as mobile workplace strategies.

To develop strategies that truly reflect the needs of the entire organization, portfolio optimization requires a planning core representing not just CRE, but stakeholder groups such as business units, Human Resources and Finance.
Most importantly, if CRE doesn’t have a direct connection to the C-Suite, it is critical to include a business partner or individual that can be close to the executive leadership during the planning process. Key to the development of optimization strategies is the inclusion of any third-party providers of real estate services such as occupancy planning, program and project management, transaction management and lease administration.

**How does it work?**

A critical first step in the process is to understand the corporate objectives that will impact the portfolio, a top-down information-gathering process that begins at the C-Suite. Any initiative that doesn’t include intelligence from the highest level risks failure due to information gaps. For example, it may not be prudent to put a new chiller into a building of a business that will be divested in the coming year, but such mistakes have been made by CRE groups not fully aware of decisions being made at the top of an organization.
Supply
Solid foundational data is imperative to support an effective portfolio optimization program. Information on: property locations and size in square feet, as well as number of seats, employee populations and number of square feet per seat and per employee, all play a critical “data set” role in formulating optimization strategies. It is very likely that data from these three groups will not match exactly, so it must be triangulated into a demand range for portfolio optimization modeling purposes.

This current state data is used to create a baseline for the organization’s portfolio that includes information such as:

• Capacity, population and vacancy information
• Utilization reports on how space is known to be occupied
• Projects already in progress that will affect current specifications
• Lease expirations and renewal options

Demand
The baseline is then compared against demand. Demand is gathered through multiple sources: intelligence on upcoming business initiatives collected from the C-Suite, day to day business insight from the local business units, budgeted headcount data from the finance organization and current recruiting information from the human resources group. The data found across these three sources may not match exactly, so it must be triangulated into a demand range to be used for portfolio optimization modeling purposes. CRE should develop 3-5 different scenarios, including space need explanations and action plans covering:

• No changes made
• Conservative space approach toward future business goals
• “Middle of the road” approach
• Aggressive portfolio strategy to best accommodate forecast changes

The end result is a multi-year roadmap or a plan of record that helps drive individual real estate decisions within the portfolio. It should provide definitive information on overall corporate objectives, along with directives on how to optimize the portfolio to meet the stated objectives. For example, one
mandate might be that before a business authorizes a new lease, occupancy planning expertise must be engaged to investigate all available options within the existing portfolio. The plan of record helps improve decision making since individuals aren’t taking episodic actions that work against the larger goals of the organization. The focus is looking beyond tomorrow at the long term and, as such, the plan of record should ideally lay out strategy 3-5 years into the future. The payout will take time, but it is well worth the effort to build a portfolio that fully supports the objectives of the business and at the best possible cost.

Finally, portfolio optimization is an ongoing activity that when engaged, delivers the appropriate platform for the enterprise to conduct its business while ensuring the elimination of unnecessary space and expense.

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