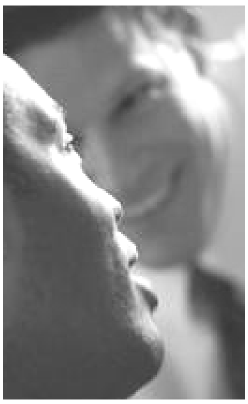


relationship capital

Is the property sector ready for it?

A range of influencing factors – not least the current economic climate – suggest that the supply-side domination of the UK property market will change over the next few years. A new property business model is needed if owners are to maximise income from their investments and achieve the holy grail of increased 'tenant stickiness'.

CBRE has commissioned a significant piece of research to probe tenant psychology and identify new approaches for its clients. The findings are clear: first movers may gain significant strategic advantage by investing in the development of 'relationship capital'. But is the Property sector ready for it?

the research

A large scale qualitative research programme was delivered on behalf of CBRE by strategy consultancy *forward thinking inc* between May and July 2008. In-depth interviews were carried out with property heads and senior managers in 60 UK organisations occupying offices or industrial space. The respondents, who were recruited by *fti* and were not informed of the identity of the research sponsor, were from a range of industry sectors and geographical locations and ranged from SME's to major multinationals. (See Box 1)

the findings – tenant needs

The research shows clearly that most tenants do not believe that landlords or their agents understand their needs well. Worse, they believe that little *attempt* is made to understand them – and how the property they are occupying fits in with their business strategies. The research highlights 8 specific issue areas.

1 Business understanding

For landlords, the building is an asset on which to maximise return. But for tenants – their customers – the building is simply an *enabler* in the execution of their business strategy. Tenants want landlords to better understand their business and the building's role in delivering results.

'It's important that landlords understand our business needs – it shows they respect us and care ... it's a basic human need. At least show an interest, make an effort!'

(Major firm of architects)

2 Brand understanding

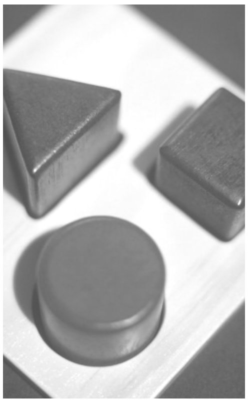
Landlords too often forget that a tenant's property reflects their brand to many audiences – employees and potential employees, customers, suppliers and other visitors. Property is a critical communication medium and tenants are becoming increasingly sophisticated in their understanding of its impact.

'Our workplace reflects our brand. I'd like the landlord to understand our brand positioning and how the building and the way it runs can impact brand communication. Quite an exciting idea, actually.'

(Major telecoms provider)

Independent research from forward thinking inc commissioned by CB Richard Ellis






3 Transparency

Tenants are demanding more transparency in the relationship – something that is demanded of them by *their* customers.

'Service charge reconciliations wind me up no end. I don't accept it's an industry norm. There should be a professionally-based approach using KPIs.' **(Major bank)**

4 Predictability

The unpredictability of property transactions mitigates against effective business planning for tenants.

'From a business perspective, certainty is everything.' **(Major bank)**

5 Speed

Speed is a prerequisite for modern business, but property transactions seem almost designed to take as long as possible.

'Too much time is taken by default. It's inefficiency plus a degree of "this is the way we've always done it." Everything is done by correspondence rather than sitting down round a table and resolving things together at one time.' **(Major building supplies firm)**

6 Cost control

Tenants believe that the property management process carries unnecessary cost – particularly the 'time cost' of process complexity. Key problems are:

a the over-use of lawyers

'There's a huge amount of time wasted on changes that were not wanted by the landlord being made through sheer lack of understanding and arrogance on the part of the lawyers.' **(Major broadcaster)**

b lost assignments

'Assignment is always a problem because our name is one of value. They're not happy if it's Joe Bloggs ... they're obstructive. We lose assignees because so much time gets wasted.' **(Major broadcaster)**

c dilapidations

'I'd describe it as legalised extortion ... it's simply a method of extracting cash from occupiers. We're able to field professionals to fight it, but small occupiers are taken for a ride.' **(Major bank)**

7 Empathy

It is possible to create great empathy with minimal cost. In a process driven, sometimes adversarial, relationship, 'random acts of kindness' have a disproportionately positive effect.

'An occasional gesture, an indication that they understand that we are real people with real pressures, is worth a lot. At renewal time, you remember these things.'

(Small management consultancy)

8 Trust

Levels of trust in the landlord / tenant relationship are – not surprisingly – very low.

'What adds cost is the lack of trust in this industry. It would be great if we had an open relationship with landlords and built a level of trust between us; at the moment, they're trying to screw money out of us; we're trying to get something for nothing.'

(Major telecoms provider)

Box 1 - respondents

Financial Services
ABN AMRO
Alchemy
Deutsche Bank
ING
Investec
Lloyds TSB
Nationwide
UBS
Zurich

Professional Services
BDP
Coussins Associates
Gensler
Nabarro
White & Case

Media / Telecoms
BBC
BSkyB
BT
Experian
Orange
Pourshins
Virtual IT

Corporate HQ
Environment Agency
Food Standards Agency
GfK NOP
Herman Miller
Lufthansa
Rio Tinto

Building supplies
Alloway Timber
Jewson
Travis Perkins
Wolseley

Logistics / Storage
Big Yellow
Deugro
James Fisher & Sons
G4S
Lok 'n Store
Stobart Group
SKW
TNT
World Freight Centre

Manufacturing
Bakkavor
Colourzone
De Wintons
Field Group
Fusion Glass
Phoenix

Other
Big Active
Interserve
Lindner-Schmidlin
Pastest
Swinton Insurance
Synapps
Virgo
Zumtobel

Property professionals
Chartmicro
eOffice
Glenmhor
Invista
Marriott

the findings – key pressure points

The research gives a clear insight into what is important to tenants and to their frustrations with the way things currently work. Clearly, a simple start point in executing a better relationship strategy will be to take action to change perceptions in these 8 areas. The research also highlighted the key pressure points in the relationship. These are the occasions when positive action or changed behaviours on the landlord side have maximum potential to create a positive impact on tenant perceptions and the landlord / tenant relationship. They are listed here and ranked in terms of impact potential, based on the interviews.

1. Alterations
2. Service charge
3. Rent reviews
4. Dilapidations
5. Assignment
6. Start of relationship
   – moving in
   – landlord change

key insight – 'a relationship vacuum'

The research suggests a 'relationship vacuum' which is of concern in itself given the benefits of keeping good tenants in place for as long as possible. Moreover, the finding comes at a time when customer relationships and the concept of 'relationship capital' is seen as an increasingly powerful driver of corporate value. Most analysts argue that across the majority of business sectors, intangible assets (primarily brand, people and intellectual property) rather than a company's physical assets drive value. One research study shows that whereas in 1975, typically 10% of market capitalisation values were driven by intangibles, today the figure is closer to 70%.

relationship capital

A key component of the intangible asset base is 'relationship capital' which is that value tied up in positive relationships with customers, employees and suppliers. Because it is recognised as a critical value driver, firms are becoming increasingly focused on developing strategies to deliver it.

The property sector certainly appears to lag the market in this respect.

- → Leases expiring in 2007, av. % vacant at year end 57, up from 38 in 2006
- → Leases containing a break in 2007, av. % of breaks exercised and vacant at year end 29, up from 24 in 2006
- → 57% of units void at the end of 2007 – highest figure recorded in 10 years

Source: Strutt & Parker IPD Lease Events Review 2008

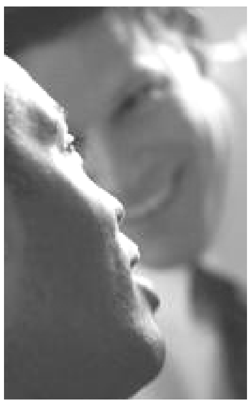
property values

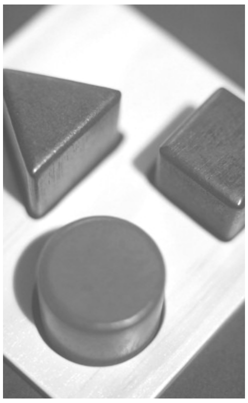
In the UK property sector, several factors appear to have mitigated against the development of 'relationship capital'. Psychologically, it could be argued that the physical / financial asset has dominated thinking. In addition, the business system and institutional approach to leasing have tended to lock customers in to long term relationships, whilst, finally, supply side domination has meant that growth in capital value and income have in the past been achieved without the need to pay too much attention to the intangibles.

economic costs

Aside from the potential longer term positive impact of stronger customer relationships on asset value, the short term economic consequences of a poor relationship are increasingly stark.

The commercial argument is clear, an empty building is an under-leveraged asset. The costs of poor relationship management in terms of lost income, re-letting costs and management time are significant and rising (see box opposite).

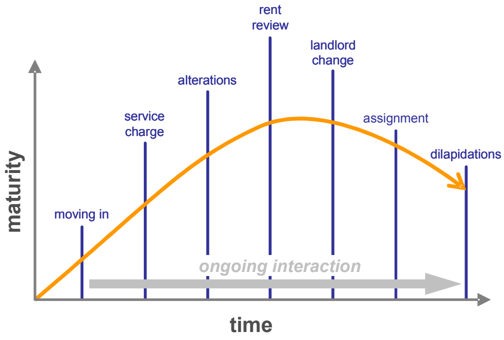




a way forward

using the lease lifecycle as a framework

lease lifecycle



Professional marketers are well versed in the concept of the product lifecycle. They manage to extend the curve of a product's life via a series of pre-emptive interventions.

In just the same way, every property lease goes through a natural cycle which provides a framework for just such a series of pre-emptive interventions.

segmentation as a critical tool

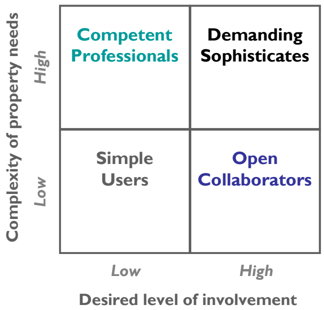
In executing effective customer relationship strategies, the key in most industry sectors is the effective segmentation of customers into discrete sectors and the development of specific strategies for each. In the property sector, segmentation practices appear to be more rudimentary.

Currently, tenants are often only categorised by basic functional criteria such as geography, size and industry sector.

The key to developing a successful customer relationship management strategy, however, is to focus more on the higher order, and more differentiating, 'emotional' needs (attitudes and behaviours). This will allow a more sophisticated segmentation which can lead to tailored strategies for specific customer clusters.

Early work, as part of this research exercise, suggests a simple two axis model based, for example, on complexity of property need and desired level of involvement with landlord / agent. Most companies surveyed fitted comfortably into one of four segments. Each suggests a particular strategic stance from the landlord, an appropriate level of investment and has implications for how agents organise themselves to best serve specific segments.

customer segmentation model



conclusion

The research suggests that tenant psychology and tenant needs are currently less than perfectly understood. There is a clear opportunity to create a stronger, more enduring relationship by treating tenants as 'customers' and managing the relationship in a more strategic way. In doing so, not only are there likely to be immediate benefits in minimising voids and related costs, but also longer term benefits in terms of building 'relationship capital' and strengthening the intangible asset base. Clearly, this is not a concept which applies to all holders of property assets, but the principle of the long term benefits which accrue from well founded strategic relationships with customers, should apply.

In executing strategies designed to increase tenant 'stickiness' and build long term relationship capital, it will be necessary to carefully organise resources and acquire the organisational competencies to meet customer needs most effectively. Two models are likely to prove helpful: firstly, the use of the lease lifecycle as a framework within which to plan the execution of positive interventions in the relationship; secondly, the development of an effective customer segmentation model which allows the execution of CRM strategies targeted tightly to the needs of specific clusters of customers.

For further information about this research, please contact
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