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Strategies for Workspace Downsizing in Uncertain Times

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Graham Kirkwood from Workspace Planning Consultancy, Resource, looks at ways that companies can reduce occupancy cost rapidly in times of uncertainty, and position the organisation for the future.

Consolidating office space is a strategy that often follows a reduction in staff number as a result of an economic downturn, business merger or acquisition. Although the reduced cost of staff can have an instantaneous financial benefit for a business, reduction in office space will require additional time as well as capital cost, and may not achieve payback for some years. However, consolidation of office space not only presents a number of risks but also opportunities to better position the organisation for the future.

Resource was recently engaged by a leading international professional services firm to halve the amount of space they occupied in their Melbourne office. This requirement was in part a result of downsizing, but also a result of an increase in staff working from home and a pledge to go carbon neutral by the end of 2012. The organization introduced simultaneously a work from home policy, a review of office space, and an electronic hot-desking/hoteling system. The head of Australian operations issued an email to all staff explaining the initiatives:

“These initiatives will not only contribute to going green, they will enhance working conditions by providing the flexibility of working from home and potentially attract employees who are looking to work with a progressive and environmentally responsible organisation.”

When considering options to consolidate office space it is necessary to contemplate the future impact of the decision: Does the project present any future risks and opportunities? Can we learn from the last economic downturn? What strategies are there to speed up the workspace consolidation process and manage the risks? What opportunities are there to inspire employees and create a leaner and more efficient operation? What does it leave for the future?

What makes this economic cycle different

During the last economic downturn of 1990-92 massive staff cuts meant huge demands for reducing office space, yet the turnaround time and cost to off load excess office space exceeded what management expected. Back then organizations sought to consolidate leases, dispose of unwanted space and increase the workstation density through reduction of enclosed offices, with little regard for the employee. During the last recession business focus moved from revenue and asset growth to cost reduction.

This cycle is different in five ways:

1. Greater global market influence means the level of uncertainty is higher, and it is more difficult to anticipate where and how quickly change will occur.
2. Organizations are working space harder and more efficiently; office space built within the past decade is often 15m² per person or less.
3. A far greater proportion of costs are technology related: IT related costs now exceed occupancy cost.

4. Technology has enabled greater mobility and less reliance on office space, and
5. The demographic profile has transformed: The young generation X and Y represent our ability to sustain business as the baby boomers retire. Greater effort will be spent to retain the best and brightest of the next generation.

The average time spent planning space consolidation projects will be longer as organizations integrate work process, information technology and human resources to capitalize on the opportunities to position themselves for the future. Business focus will turn to innovation, responsiveness, employee engagement AND cost reduction.

The Need for Speed

The time between an announcement to downsize or merge, and the time to consolidate excess office space is often underestimated by non-property specialists. Often, as much time can be spent defining and evaluating options for executive approval, as it is spent implementing such options. The time it takes to eliminate excess space will depend upon whether the change is anticipated and planned, however anticipating and planning for change is a difficult task in times of uncertainty.

In times of high uncertainty it is necessary to define, plan and evaluate a portfolio of options, all of which can offer significant payback once uncertainty diminishes. By defining, planning and evaluating a portfolio of options during periods of uncertainty, it is possible to significantly reduce the time required to implement workspace consolidation projects. In effect, having a portfolio of options ready to go is a form of risk hedging, where you merely need to call the option once conditions reach a specific level.

Defining Options

Reducing occupancy costs is most often about reducing the amount of space that is leased, however as leases often have some time to run to expiry, there are risks and costs associated with sub-leasing or disposing of small pockets of space. It may be easier to dispose of the entire lease or renegotiate an existing lease on the basis of extending the lease beyond the expiry date. Key to all of these strategies is determining how much space is required, and the cost of moving people to a new or reconfigured space. Options will need to be defined, costed and evaluated against the risks and benefits. The top ten factors to consider include:

- Future headcount and growth options
- Current Occupancy cost, Space efficiencies, quality and utilization
- Lease expiry and negotiation options
- Future IT and data management upgrades or integration
- Functional relationships between business groups and that of suppliers and customers and levels of mobility
- Work Process innovations and efficiencies
- Work from home and hot desking opportunities
- Duplication of support services and infrastructure
- Project Implementation time and disruption
- Employee engagement and retention

Project options, once identified, are able to be compared according to traditional Payback, Net Present Value and Internal Rates of Return, having regard for occupancy cost savings, risks, capital expenditure and strategic value.

Resource is regularly engaged to measure costs and benefits of various consolidation projects. On several occasions we have identified Internal Rates of Return (IRR) of nearly 100%. Such benefit is cumulative over the life of the tenancy, and when discounted to present value, can far outweigh the initial capital outlay. Reduced occupancy cost is only one of the benefits measured. We also measure reduced cost of churn (ongoing workspace reconfiguration) information management, and intangible measures such as improved customer value, brand and employee equity and perceived productivity.

Resource was engaged to advise on workspace strategies to one of the major mining and exploration companies for their head office tenancy which was built a decade earlier. The lease was nearing expiry and a number of refurbishment options were being considered. A simple measurement of square metres per person revealed that the existing space exceeded 35 m² per person, compared to their competitors who were achieving less than 18 m² per person. This simple evaluation was presented to the board and a decision was quickly made not to consolidate the existing space, but rather to seek to secure a new lease in a new building.

Project Implementation

In a perfect world traditional methods of project evaluation are sufficient, however during uncertain times some decisions may need to be deferred as the level of uncertainty makes any decision too risky. Any given business will know how much change can be tolerated before an investment decision must finally be made. How much can be tolerated depends upon two factors: Firstly, the level of risk and cost impact on the business and secondly time - how long we can defer a decision before options expire. This can be referred to as a measure of volatility. Volatility diminishes as time passes because conditions become more certain.

Priority projects are those that offer both significant returns/early payback, and low volatility where the business future is certain and the decision is imminent. Where uncertainty remains, the cost of implementing any investment project can become compromised if the eventual business outcome changes.

Figure 1 below compares Volatility of project options with the anticipated return on investment (IRR or NPV) for any investment project.

Seeking Forgiveness

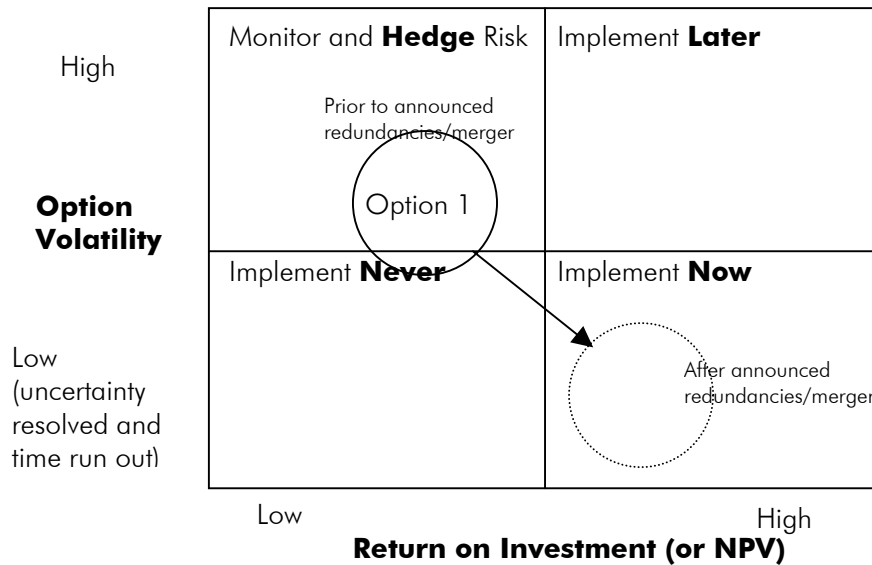
As the saying goes "Loyalty is forged in hard times not good times" During any period of change, if employees are not engaged there can be a negative impact on productivity and effectiveness. Following a significant downsizing, negative effects can be debilitating and result in loss of loyalty and employee disengagement. However there is always a positive: if change is communicated sensitively it can reinforce employee engagement or at least be met with forgiveness. Sample opportunities include:

- Upgrade of facilities, infrastructure and equipment (at competitive prices)
- Introduction of new technology that makes work easier and more efficient

- Introduction of new efficient and sustainable work practices
- Greater levels of work flexibility and mobility.

Often we find that through the briefing process, other benefits and innovations are suggested by employees that have not yet been considered.

Figure 1: Volatility/Return Matrix¹



Conclusion

Reducing occupancy costs during this economic cycle will be different and more challenging than experienced during the last recession. Real estate decisions will be far more integrated with Information Technology, Finance and Human Resource management issues. Through developing a portfolio of well considered and planned options ready to go, the time required to implement, the cost and the risks are significantly reduced. Most importantly, expectations of senior executives and employees will be better managed, and the solutions will potentially leave the organization in a better position to respond to future opportunities and growth.

The best options are those that not only reduce occupancy costs but also contribute other positive benefits to the business.

Graham Kirkwood is a Director of Workspace Strategy at Resource. Resource helps organisations to get more out of their workspace investment, providing advisory, space planning and design services. Tel 03 9604 6666

¹ Matrix is a derivation from Timothy Luehrman "Strategy as a Portfolio of Real Options" Harvard Business Review, September-October 1998