

THE ELEPHANT IN THE CORNER:

How Forward-Thinking Corporate Real Estate
Departments are Using the Labor Issue to Reduce Costs
and Improve Performance Enterprise-Wide



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With the US economy back in full swing, corporate real estate departments are under increasing pressure to look outside the traditional real estate lens to help solve the operating group's biggest challenge: sourcing cost-effective, high-quality labor.

Labor is at the heart of most corporation's ability to successfully compete in today's marketplace. It is often a company's biggest asset, while also being its biggest cost. And as businesses continue to be challenged with the dwindling supply and higher costs of today's robust labor markets, they are demanding *labor-centric* solutions from their real estate department.

"By focusing on the labor issue, rather than more traditional real estate strategies, corporate RE departments are making huge bottom-line impact and creating value that can be measured in earnings per share."

In a typical labor-intensive operation, such as a call center or back-office operation, the payroll costs can be upwards of 70 percent of the facility's overall operating costs. From a cost-cutting perspective, labor can create the largest impact by far. But too often real estate departments are treating it as the "elephant-in-the-corner," because they lack the appropriate analytical tools required to find the optimal balance between lower cost labor and *qualified* labor. Before delving into the analytics behind sourcing an optimal labor market, it is important to understand the operational savings impact.

The Savings Impact

The chart below compares the labor cost arbitrage between locating a 500-employee back-office operation in Atlanta, GA versus Huntsville, AL. The example uses a hypothetical wage differential of just \$1.00/hr (a conservative estimate) and a hypothetical reduction in turnover of 50 percent. We can predict lower turnover in Huntsville, due to fewer labor competitors in the area and greater wage impact compared to Atlanta. Recruitment and training costs have been conservatively estimated at \$5,000 per employee.

City	Employees	Hourly Wage	Annual Payroll	Turnover	Turnover Costs	Totals
Atlanta, GA	500	\$11.00	\$11,440,000	40%	\$1,000,000	\$12,440,000
Huntsville, AL	500	\$10.00	\$10,400,000	20%	\$500,000	\$10,900,000
Annual Savings			\$1,040,000	20%	\$500,000	\$1,540,000
Total Savings over 10 Year Lease						\$15,400,000

With more than a \$15 million savings over 10 years, the impact on operating costs dwarfs what can be achieved through more traditional real estate strategies. To illustrate the savings impact on labor versus real estate, consider the following:

Using a typical back-office ratio of 1 person per 125 square feet of premises, a 500 employee operation is 62,500 SF. As identified above, the annual payroll savings, per shift, using just \$1.00/hr labor savings equals \$1,040,000 (2,080 hrs/yr X \$1.00/hr X 500 employees = \$1,040,000 per shift). *To achieve the same savings on the rental rate, the company would have to negotiate a savings of \$16.64/SF on the lease rate (\$1,040,000/62,500 SF = \$16.64/SF).* That type of savings is virtually unattainable through rent reduction, no matter how good a negotiator your broker may be.

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The Performance Impact

While the savings impact of finding the right labor market is substantial and quantifiable, it is certainly not the only benefit nor is it necessarily the biggest benefit. The quality and skills of the available applicant pool are a key determinant in an operation's performance. Because, whether it's a call center defined by client satisfaction, a brokerage office defined by sales generation and quality advice, or a manufacturing plant defined by efficiency metrics, the common denominator is labor. Sourcing a labor base that has high concentrations of the requisite skills is crucial not just to the local operation, but to the entire business enterprise.

"Forward-thinking real estate departments understand that they can offer more to the corporation than simply sighting the bricks and mortar: they can play a key role in tapping the corporation into the right talent pools."

Labor-Centric Real Estate Solutions

CBRE's specialty practice group, the Labor Analytics Group ("LAG"), has assisted hundreds of corporations in re-aligning their location decision metrics from being driven by traditional real estate metrics, such as lease rollovers and facility cost reduction, to labor metrics, such as skill-based demographic modeling and wage-gap analysis.

For years the group focused its consulting efforts on the labor-intensive call center and back-office industry— helping Fortune 500 companies source lower cost, yet higher performing labor in rural and third tier markets. However, as its clients labor requirements grew more sophisticated, so did the group's ability to model more specialized skill sets. Currently, the group's

Sourcing Quality Labor: Segmentation

labor consulting services ranges from sourcing specialized healthcare skills, such as nurses and pharmacists, to highly-experienced financial services skills, such as Series 6 & 7 Licensees.

The group continues to innovate new, more accurate methods of analyzing labor markets and tapping talent pools. It's Segmentation Analysis and Workforce Longevity Model are just two of the most recent tools the group has developed to more accurately assess and target its clients labor force.

The biggest hurdle in location analysis is drawing the link between available statistical data and operational performance. For instance, do high educational statistics suggest anything about the work ethic of the community? Does a labor market with a disproportionately high percentage of employment in the Finance, Insurance and Real Estate industries mean better skilled claims adjusters? Are low median household income levels any indicator of employee attrition? While traditional data points such as these can be useful in assessing labor supply and cost, when it comes time to assess the quality and performance of a labor market, these demographics fall short.

A better method is to work backward by modeling an existing operation's top performers. Although it may be an over-utilized term, reverse-engineering to identify future top performers is an excellent way of drawing the link between demographic characteristics and operational performance.

However, simply reverse-engineering the top performers is not enough. A successful project relies on utilizing a mosaic of data types that include more than just traditional Bureau of Labor Statistics demographic data. For years the retail industry has relied heavily on "segmentation data" that combines buying patterns and lifestyle habits with more traditional demographics, to



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identify groups of people that share the same behavioral patterns. Retailers have found that by identifying the groups of their best, most loyal customers, they can increase sales through more accurate target marketing. The concept for sourcing a higher performing labor base is the same, except instead of the best customers, we are looking for the best employees.

In response to its client's struggle to source a higher performing labor base, LAG developed the Segmentation Analysis, which allows its client's to define the behavior and performance habits of their top performers across their portfolio of facilities. By analyzing these behavioral traits, LAG can identify which segments the company's top performers fall under and then benchmark thousands of locations by the degree to which their labor force has high concentrations of these segments. The analysis has the capability to locate top performers all the way down to the address level. Through this, the data can even be used by the company's recruiting department to run direct-mail hiring campaigns or advertise at restaurants and stores frequented by the top performers.

Labor Drives Location

Labor, not real estate, is the operational driver in today's location decisions and the internal operating groups in corporate America are demanding more from their real estate department. Labor continues to be at the forefront of an operations success and because payroll costs can be upwards of 70 percent of operating costs, the savings benefit to locating in more cost effective labor markets is big. Companies like GE, Verizon Wireless and Walgreen's use labor metrics not real estate metrics to drive their location decisions, because they know that tapping the right people for the job is at the heart of their competitive advantage.

Portfolio Optimization and Growth Planning: Workforce Longevity Model

One of the biggest challenges corporate real estate executives face is optimization and growth planning of the real estate portfolio. Too often, this venture is approached from a real estate perspective, rather than a real estate *and* labor perspective. Evaluating a portfolio on a more holistic basis can be a daunting task and analyzing which labor markets are appropriately positioned for growth is difficult.

In response, LAG developed an evaluation tool that can identify which of its clients operations may be in markets that would maximize their success, and which may be at risk today, or in the future. The Workforce Longevity Model analyzes several competitive, market, and client factors in order to determine the longevity of each labor market. Understanding the length at which a client can operate in each market helps them optimize their portfolio from a labor supply, competition, and wage standpoint and develop a strategy towards site selection needs going forward.

The Workforce Longevity Model is an analytical tool built to assist clients in estimating the potential length of a given labor market based on specific operational parameters (i.e. employment size, annual turnover and starting base wage rate). The model estimates the potential applicant pool in a market by factoring macro demographic data (such as labor force, population growth and unemployment rate) along with market-specific competitive data (such as competitive occupations, wage rates and turnover). By utilizing these and other factors, the model can estimate a market's labor longevity and identify the primary sources of market depletion. Once the baseline is set, the model can then conduct "what if" scenario modeling to optimize wage rates and employment levels portfolio wide.

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