PRIVATE EQUITY PERFORMANCE IMPROVEMENT

Corporate Real Estate as a Value Driver for Business Transformation and Operational Agility

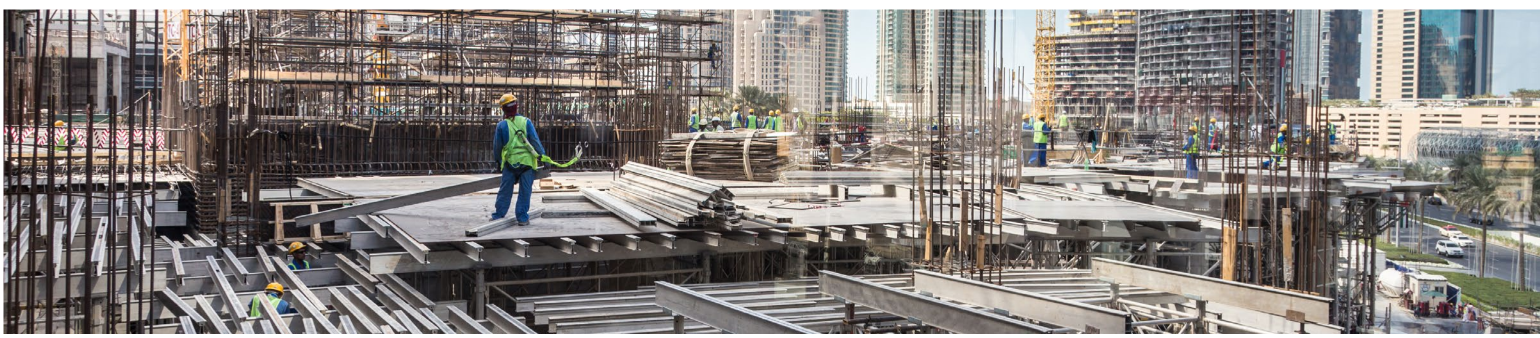
For most companies, real estate is not a core business, but nearly every enterprise must actively manage their real estate portfolio even though doing so is a complex task. With the right strategy in place, managing corporate real estate can positively impact EBITDA.

Too often, commercial real estate is perceived as a cost center rather than a value driver. Corporate leaders and private equity (PE) real estate operators can accelerate value upside by deploying strategies to leverage corporate real estate to their advantage.

The task of managing real estate goes beyond just leases, contracts, and asset acquisitions or dispositions. It also entails the proactive management of facility operational expenses, including maintenance and repair, utilities, insurance, janitorial, food service, and landscaping, among others. Changes that affect the company's operations also impact many other functions of the organization.

Corporate real estate can be used as a value creation tool by aligning business objectives and growth and reducing operating expenses through efficiency. Portfolio companies who refrain from optimizing their real estate and facility management because of its complexity and level of effort are leaving money on the table. The good news is that no matter the size of the business, companies can rapidly create value and grow it over time. To do so, they must:

- Understand the inertia of corporate real estate management
- Create discipline and rigor in the process
- Change the historical broker relationship by applying new leasing approaches
- Focus on facilities management in a smart way
- Emphasize lease restructuring
- Deploy technology and adopt AI in the right places
- Monetize non-core assets
- Consolidate real estate portfolios around geographic and organizational clusters



CHALLENGES TO CORPORATE REAL ESTATE MANAGEMENT

Procuring space and managing lease expirations are strategic levers that require proactive planning and disciplined execution. Additionally, optimizing real estate management within a company is not often conducted with a view toward either saving money or optimizing footprints.

Many companies don't have a cohesive corporate real estate strategy in place to analyze and improve office, production, and customer-facing spaces that fit the needs of the business or align with the future growth opportunities the business is striving toward. To create value, corporate real estate strategies must align with the overall business strategy.

If left unattended, these challenges can entrench inefficiencies within the company, preventing businesses from realizing savings that directly impact the bottom line.

CREATE DISCIPLINE AND RIGOR IN THE PROCESS

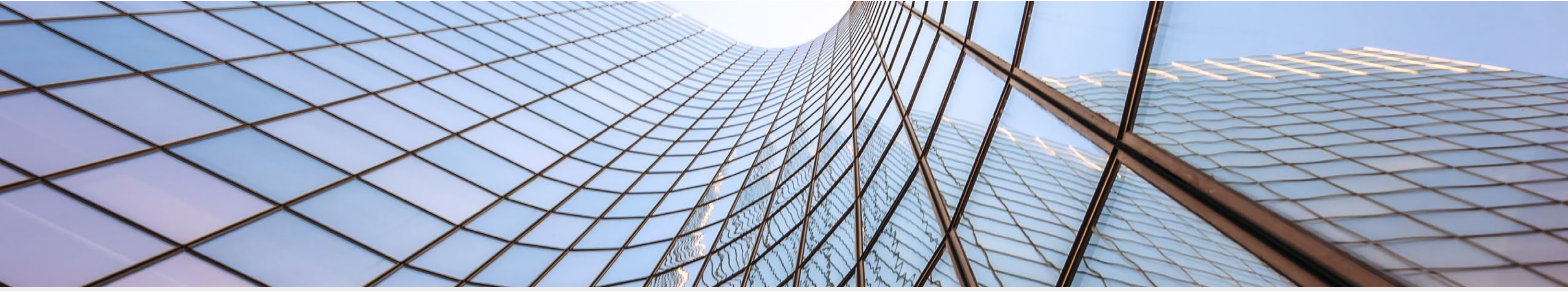
At the portfolio company level, corporate real estate and facilities management is usually less of a focal point than other organizational needs. By strategically improving processes and adhering to procedures, the result can improve margin.

No matter the business, companies must procure space and manage idiosyncratic landlords, lease expiration dates, terms, and timelines. Applying a little rigor to tracking, planning and managing this process can favor lessees.

One process that can help is to apply a strategy for approaching landlords at the optimal time. Most lessees wait until it's almost too late to renew or simply exercise their renewal option, but they're missing out on negotiating better terms and losing leverage. Landlords typically have more leverage when they are approached close to lease expirations. Having a system in place to start lease renegotiation and renewal conversations 12-18 months before key dates can help companies create a leverage case to win concessions or interpolate other options.

Typical lease durations are long; a robust real estate management process can provide cost savings and efficiencies across these long terms. Leveraging staggered lease expirations, where a portion of the portfolio turns over regularly, creates a structured process for lease reviews, stakeholder engagement, expert involvement, and prioritization of critical terms, driving greater portfolio value and stronger alignment with business strategy. What can your company do to enhance diligence in managing your real estate to improve efficiency and costs? Forming solid processes and procedures in advance prepares you to be agile when opportunities arise and ensures the important clauses and terms are fully baked, enabling the organization to take advantage of new space in the market or sudden vacancies.

Closely aligning with operations on future plans and requirements and establishing rigor over the corporate real estate process allows the real estate team to be active in the market, understanding the market trends that will enable corporate real estate to deliver the right solution for the business at the best value.



STOP THE BROKER BONANZA

Companies often have relationships with multiple commercial brokerages across their global portfolios. With this, the landscape is already fragmented and very much driven by local brokers when it comes to negotiate space, and that broker may also be working for the landlord. From the start, each transaction tends to be broker-led and often results in larger space for a larger commission. In other words, this process is not in your company's best interest.

This can start with a detailed inventory of all the terms and conditions, rent amounts, and expiration dates on all leases and assessing any patterns that become evident. Are certain clauses showing up time and again? Are they favorable or costly? Which properties are susceptible to market fluctuations? Companies should segment leases based on type, location, and other factors. They should come away with a negotiation strategy that's based on market research, business needs, and expected goals to maximize their position in negotiations. Utilize the corporate real estate team to define the pertinent negotiation items and requirements to form a go-to-market or leasing strategy and utilize the brokers to tactically execute it. This will drive value and enable corporate real estate to provide the best product to the organization.

In many cases, the higher the number of locations the more leverage a company has. To take advantage of that, a team within the organization should begin to create and build strong relationships with tenant brokers who have experience handling muti-location negotiations. Tenant brokers work for you, not the landlord, so they can work on your behalf to obtain more favorable terms. The complexity of negotiating multiple leases across markets also requires qualified professionals with real estate expertise to review and identify problematic clauses or terms.

Like procurement strategies, utilize the power of the PE's portfolio to establish a critical mass in the real estate portfolio. This will drive value through better commission structures and better broker resources that can negotiate more advantageous deals.

FOCUS ON SMART FACILITY MANAGEMENT

Companies have two cost centers with property: rent and non-rent. These cover a host of areas, including utilities, maintenance, cleaning, security, food service, safety and compliance, and capital improvements like upgrades or repairs. Getting a handle on all of these to effectively manage costs can be difficult.

Portfolio companies tend to be smaller in scale, so an integrated facilities management model may seem too complex for them to handle and can take too long to implement. But it doesn't require a long, drawn-out effort to understand how portfolio companies can build efficiency in facilities management.

Utilizing a data-forward approach with how they intend to manage properties and operational needs, companies can reduce complexity and embrace the challenge. How do companies know they're spending too much in certain areas? The key is data.

One of the biggest challenges of cutting expenses is to identify the leakage. Too many companies simply don't know they have excess spending. Contract negotiations and agreements can be signed without including a competitive bid process, requirements may not be properly defined, service-level agreements can be hard to enforce, and automatic renewals can occur without review. Gathering and normalizing existing cost data, such as vendor payments and terms within leases and contract agreements, provides enough data to be analyzed rapidly through emerging technologies. Once a picture of expenses and terms is formed, it can be benchmarked against other companies and properties.

Done correctly, PEs can quickly get a handle on excess spend and begin to plug holes in the operating expense wall. This approach, as opposed to a fully-integrated facilities management program that can take years to effectively implement, is aligned to the rapid results PEs with nearing exit horizons seek. Done across multi-location portfolios, this can materially impact the bottom line.

Additionally, facilities management is a prime candidate for inclusion in the PE firm's portfolio-wide procurement platforms. The corporate real estate team should define the service requirements and service levels, and the power of the centralized procurement program can be utilized to negotiate and quickly achieve cost savings.

FOCUS ON LEASE RESTRUCTURING

Automatic lease renewals can easily slip under the radar, so it's to the company's advantage to proactively restructure leases for more favorable terms that add value to the organization.

Companies should frequently revisit each lease and understand both the company's situation and that of the landlord.[1] Is the landlord in a healthy position or has the market environment deteriorated since you signed the lease? If the landscape has worsened for the landlord, which can range from high vacancies in the building or area to the location becoming less desirable for any reason, there's an opportunity to blend and extend leases.

In such cases, tenants can ask for a reduction in rent now by offering to lease for a longer term. If agreed to, this blended rate brings the overall cost down over time.

In the opposite environment, the landlord may be in a strong position with inventory maxed out and in high demand. In this case, they may be willing to forgive a company's lease with the prospect of enticing a higher paying tenant, allowing the portfolio company to exit the lease on favorable terms.

OVERALL STRATEGIES TO AFFECT EBITDA

Deploying AI and other technologies across several areas, such as facilities management, lease restructuring, and continuous benchmarking, can optimize the portfolio of properties.

Facilities management is a category where deploying AI strategies can help leadership make cost-cutting decisions faster. For instance, AI-powered systems can analyze historical and real-time sensor data to predict equipment failures before they occur. AI can also integrate with Internet of Things (IoT) sensors to monitor energy consumption, occupancy, and environmental conditions, adjusting heating, cooling, and lighting systems based on real-time data and reducing energy waste. Implementing AI can automate repetitive tasks such as work-order scheduling, vendor management, and asset tagging.

The key to an effective, data-driven solution to corporate real estate management is tracking key performance indicators and demonstrating return on investment.[2]

Another strategy that can pay dividends is to monetize core assets. If companies own properties, there may be opportunities to sell excess land or buildings or explore the divestment of property that has appreciated to then move into a lower-cost building.

Consolidating footprints can also add value that continues into the future. By clustering locations by geography or function, companies may leverage opportunities to reduce other costs, such as transportation or warehousing, among others.

[1]https://www.bdc.ca/en/articles-tools/money-finance/buy-lease-commercial-real-estate/how-to-negotiate-commercial-lease-effectively

[2]https://www.realcomm.com/news/1035/2/9-corporate-real-estate-metrics-you-should-be-tracking

PE FUNDS CAN IMPROVE MARGINS THROUGH PROPERTY MANAGEMENT

The nature of portfolio company time horizons may discourage PE funds from effectively managing properties to add value, but there are tools and services available to PEs that can rapidly reduce costs. Simple processes and procedures can drive rigor around their real estate assets and enable a more successful exit of the business.

Buyers want companies that have already dealt with lease and facilities basics, meaning the underlying foundation of their purchase is stable. They may envision continued optimization under their ownership, but PE funds can benefit from better margins by building the appropriately-scaled processes and procedures to enable stability and cost management.

HOW CAN A&M HELP?

The Corporate Real Estate team in A&Ms Private Equity Performance Improvement (PEPI) division works with funds and investors to continually add value to companies' property portfolios, focusing on bottom-line impact, operational and service excellence, and accelerated performance. Blending technology with decades of experience across multiple industries, A&M helps clients enhance efficiencies in their portfolio companies to create better margins on a sustainable basis.

Together with other integrated service teams within PEPI, A&M offers deep experience in running exit-readiness programs and positioning businesses for sale based on a robust operating plan.

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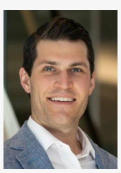

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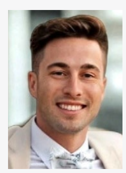

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