Decision-Making Criteria for the Acquisition of Office Buildings

Do building features decide?

Graduation Presentation
April 16th 2010
Rodiaan Gijselaar
ORGANISATION

Student:
Rodiaan Gijselaar

1st Mentor:
Drs. J.P. Soeter (Building Economics)

2nd Mentor:
Dr. C.L. van Oel (Methodology)

Representative:
Dr. J.L. Heintz (Design Management)

Graduation Company:
Ir. J. Buijs
CONTENT

• Introduction
• Methodology
• Findings
• Conclusions
Decision-Making Criteria for the Acquisition of Office Buildings

Do building features decide?

INTRODUCTION
INTRODUCTION

Problem definition

• Economic crisis hit real estate market
• More critical decision-making by investors
• Underlying value becomes important
• “Location, Location, Location”??
Relevance

"Tenants have become more articulate and they have more critical aspects on which they assess an objects’ potential”

“I expect all parties in the Netherlands, as well as in other Western European countries, to focus on the physical aspects in the future”

"From Excel-sheets back to bricks”

“Other than at top locations, other factors will play a more important role”

Quotes from Peter van der Zande (VastNed O/I) and Bas Jochims (BPF Bouwinvest)
Hypothesis

The **building features** are of such importance to the **net rental income** of an office building that it needs to be considered as a **decision-making criterion** in the **acquisition strategy** of an institutional real estate investor.

- **Building features** = physical features at building level
- **Net rental income** = performance of an office building
- **Decision-making criterion** = what criteria to use
- **Acquisition strategy** = which building to choose
Research question

Which **physical office building features** are to be distinguished to improve the set of **decision-making criteria** for the **acquisition** of office buildings by institutional real estate investors?

What recommendations can be made to implement these features into an **acquisition strategy**?
Sub questions

1. What criteria are currently applied?
2. What are influencing factors of an office building?
3. To what extent do they influence performance?
4. What should an investor do with this information?
INTRODUCTION

METHODOLOGY

FINDINGS

CONCLUSIONS

Currently applied

ING Real Estate portfolio assessment model

- Quality of the location: 45%
- Regional market: 25%
- Quality of the building: 20%
- Age: 10%
Decision-Making Criteria for the Acquisition of Office Buildings

Do building features decide?

METHODOLOGY
METHODOLOGY

- 119 office buildings
- 2000 - 2009
- National spread
- Secondary locations
- Size: 290 m² – 25,000 m²
- Value: € 0.4 – € 36.0 mln
### Used data

<table>
<thead>
<tr>
<th>Regional Market features</th>
<th>Location features</th>
<th>Building features</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market supply</td>
<td>Position with respect to Randstad area</td>
<td>Age</td>
</tr>
<tr>
<td>Market absorption</td>
<td>Urbanization class</td>
<td>LFA / GFA Ratio</td>
</tr>
<tr>
<td>Market office stock</td>
<td>Number of residents in place of location</td>
<td>Number of floors</td>
</tr>
<tr>
<td>Market office stock in use</td>
<td>Location type surroundings</td>
<td>Average Lettable Floor Area per Floor</td>
</tr>
<tr>
<td>Regional vacancy rate</td>
<td>Distance to NS Station</td>
<td>Using typography</td>
</tr>
<tr>
<td>Regional prime rents</td>
<td>Distance to Highway</td>
<td>Flexibility in lay-out office building</td>
</tr>
<tr>
<td>Regional lowest rents</td>
<td>Distance to Public Transport</td>
<td>Mixed use of functions in the building?</td>
</tr>
<tr>
<td>GDP</td>
<td>Number of parking places</td>
<td>Free standing</td>
</tr>
<tr>
<td>Employment volume</td>
<td>Parking norm (m² LFA per parking place)</td>
<td>Facade materials</td>
</tr>
</tbody>
</table>

- Shape of the buildings facade
- Building type
- Shape of the footprint of the building
- Spatial lay-out
- Charisma entrance inside
- Charisma entrance outside
Decision-Making Criteria for the Acquisition of Office Buildings

Do building features decide?

Building features

INTRODUCTION

METHODOLOGY

FINDINGS

CONCLUSIONS
Building features
Regression modelling

**Outcome**$_i = \text{Model}_i + \text{error}_i$

$Y_i = \beta_0 + \beta_1 X_i + \epsilon_i$

$Y_i = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \ldots + \beta_n X_n + \epsilon_i$
Regression modelling

\[ \text{Net Rental Income} = \beta_0 + \beta_1 \text{Regional Market Features}_i + \beta_2 \text{Location Features}_i + \beta_3 \text{Building Features}_i + \epsilon_i \]
Decision-Making Criteria for the Acquisition of Office Buildings

Do building features decide?

FINDINGS
FINDINGS

If not at top location:

• Performance strongly influenced by building characteristics
• Location not as important as presumed
Building features

↑ “Age” = ↓ performance
Decision-Making Criteria for the Acquisition of Office Buildings
Do building features decide?

Building features

“Nr. floors” = performance
Building features

“Attractive entrance” = performance
Building features

“High rise” & “complex buildings” = ↓ performance
Building features

“Single tenant” = \( \uparrow \) performance

“Medium adjustable layout” = \( \uparrow \) performance
Decision-Making Criteria for the Acquisition of Office Buildings

Do building features decide?

CONCLUSIONS
CONCLUSIONS

Decision-making criteria

- Mapping = complex:
  - Motives
  - Strategies
  - Circumstances
  - People involved
- Rules of play
Affecting features

- Factor location acts as proxy
- Building is appreciated for what it is built for
- Fitness for use determines willingness to pay
- Willingness to pay determines performance
Implications

Perfect building:

- Average size
- 3 – 6 floors
- 1000 m² average area per floor
- Attractive entrance
- New building
- Near public transport hub
- Large city
### Implications

<table>
<thead>
<tr>
<th></th>
<th>Le Verseau, Zwolle</th>
<th>High Flex Center, Maarssen</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Selected by</strong></td>
<td>selection criteria</td>
<td>opposite selection criteria</td>
</tr>
<tr>
<td><strong>Performance</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average quarterly NRI (EU/m²)</td>
<td>44.8</td>
<td>18.6</td>
</tr>
<tr>
<td><strong>Location</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Distance to public transport (m)</td>
<td>400</td>
<td>200</td>
</tr>
<tr>
<td>Number of residents in place of location</td>
<td>118,192</td>
<td>39,647</td>
</tr>
<tr>
<td>Location in relation to Randstad</td>
<td>Outside Randstad</td>
<td>Inner Randstad</td>
</tr>
<tr>
<td><strong>Building features</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Charisma entrance inside</td>
<td>Attractive</td>
<td>Unattractive</td>
</tr>
<tr>
<td>Building type</td>
<td>Basic</td>
<td>Complex</td>
</tr>
<tr>
<td>Using typology</td>
<td>Single tenant</td>
<td>Multi tenant</td>
</tr>
<tr>
<td>Flexibility lay-out</td>
<td>Medium Adjustable</td>
<td>Very adjustable</td>
</tr>
<tr>
<td>Number of floors</td>
<td>6</td>
<td>2</td>
</tr>
<tr>
<td>Average LFA per floor (m²)</td>
<td>1208</td>
<td>1654</td>
</tr>
<tr>
<td>Current age (yrs)</td>
<td>5</td>
<td>20</td>
</tr>
</tbody>
</table>
Implications

Performance (NRI)

- Le Verseau, Zwolle
- High Flex Center, Maarssen
Reservations and Limitations

- Only non primary locations
- Few peculiarities in NSI portfolio
- Difficult to match with existing literature
- Limited resources
- No sustainability
Recommendations for the industry

“Location, Location, Location”

“Location, Building, Quality”

- Make distinction in primary and non primary locations
- Focus on large 4 cities or large cities outside Randstad
- Do not focus on “High Rise” or “Complex” properties
Recommendations for NSI

- Add building features as criteria to currently employed set
- In the Randstad focus on large 4
- Outside the Randstad maintain criteria of > 60,000 residents
- Continue disposition buildings less € 5 mln book value
- Be careful with above average projects (such as “La Tour”)

Recommendations for NSI

- Repeat research within 5 yrs considering contract expirations
Recommendations for further research

- Repeat research with:
  - Same type of dataset
  - Extension with primary locations

- Ex ante research to provide for future implications

- Diversification research at building feature level
The **building features** are of such importance to the **net rental income** of an office building that it needs to be considered as a **decision-making criterion** for the **acquisition strategy** of an institutional real estate investor.

- Building features are important
- They must be considered as decision-making criteria
- It will influence the acquisition strategy
Decision-Making Criteria for the Acquisition of Office Buildings

*Do building features decide?*