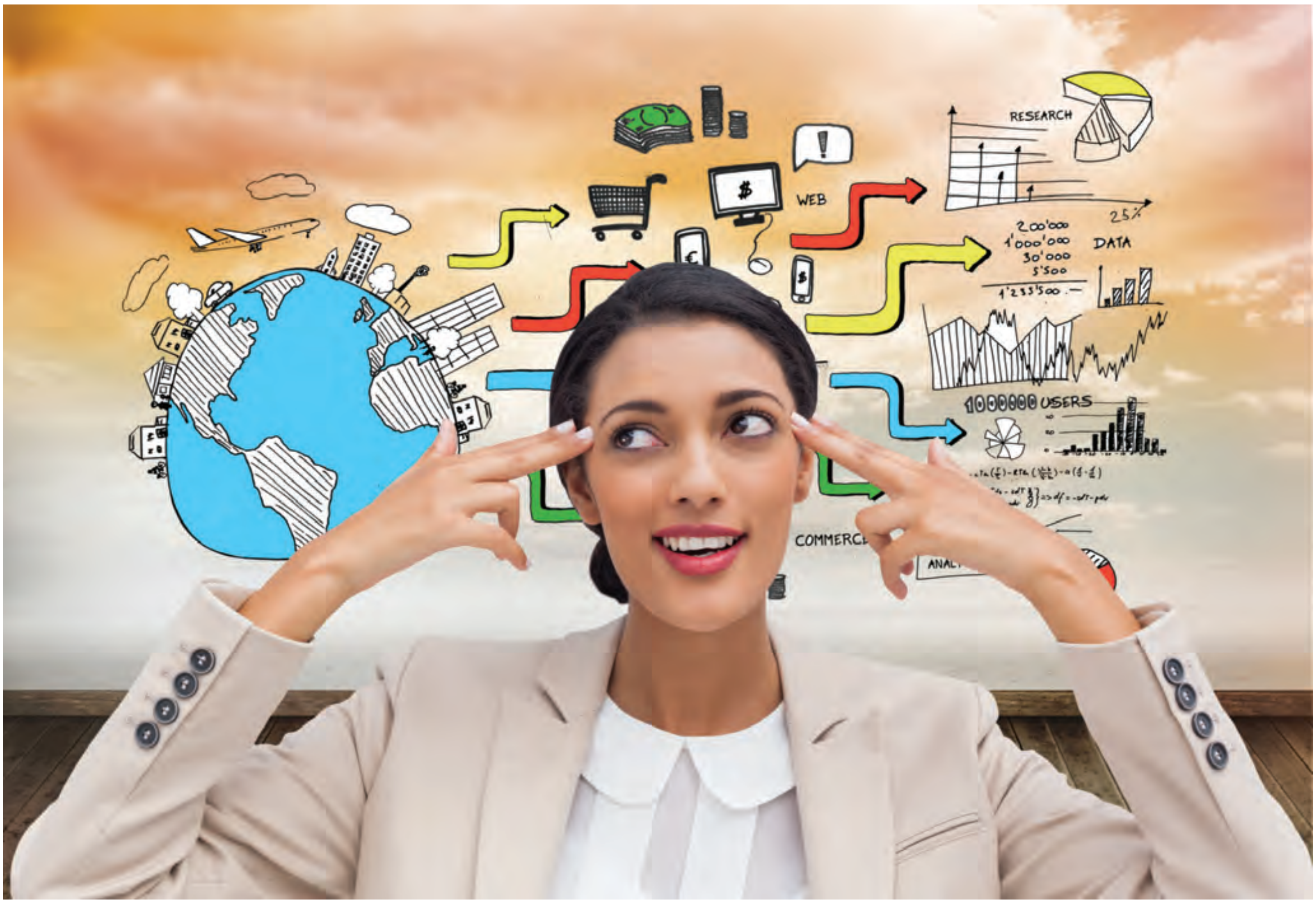


E-everything

Tech innovations are shaping how business is done anywhere and everywhere

by Dr Jennifer Molloy

The fast pace of electronic innovation is akin to transformations that occur in geologic time: if you blink, you just might miss exactly what they are, but not their impact on the world. The ties between how we work, do business and live our lives are becoming more integrated as technological advancements allow us to blur previous divisions between life, work and play. And these innovations are steadily affecting brick-and-mortar investments in some subtle and not-so-subtle ways. What are some of the current effects of technological innovation on the office, retail and industrial sectors? And what do real estate investors need to know to keep ahead — and stay protected — in the digital age?

Work here, there and everywhere

It is no secret that telecommuting and mobile computing are reshaping how people work, but the important question for office landlords and developers to consider is how such changes are affecting demand for space as well as design requirements for that space, says Marc-André Flageole, a portfolio manager with Presima. The trends toward "hot desking" and activity-based office layouts are seeing a number of large firms throughout Asia Pacific using mobile technology to help do away with designated office space in favour of being able to connect and work from anywhere within a defined activity zone. With a certain number of employees expected to be out of an office on any given day, tenant space requirements dwindle by 20–40 percent through the use of such mobile computing in the office, according to data estimates.

"If implemented in an increasing number of firms, these could ultimately have a significant impact on the need for office real estate," Flageole notes.

Are such trends destined to become the norm in the office sector? At this point, they certainly are increasing, and more so in EMEA and the Asia Pacific region than in North America. According to Cushman & Wakefield's 2013/2014 *Workplace Transformation Survey: A Global View of Workplace Change,* a top priority for today's office occupiers is to create corporate work environments that will maximise productivity and efficiency, and they are also taking a proactive approach regarding cost savings measures, increased efficiencies, cultural effects, and human resource benefits and challenge.

The survey's main findings are:

1. More occupiers globally are implementing workplace transformation programmes.
2. On average, occupiers cited human resource factors (eg, recruiting, workforce productivity and improved work/life balance) over cost factors, such as reduced facility costs and lower churn as drivers of workplace change — but both were important to occupiers.
3. Hotelling (ie, reservation-based unassigned seating) strategies are being more rapidly employed in EMEA and Asia Pacific than North America.
4. Reluctance of company management ranks as the biggest barrier to workplace transformation.
5. Most workplace change strategies are effective in helping organisations reach their goals.

While overcoming corporate culture issues represents a significant barrier to transforming the workplace environment, the Cushman & Wakefield survey suggests these cultural issues will likely continue "until it becomes clear that not embracing some form of workplace transformation becomes a competitive disadvantage." Even using technology for sustainability efforts can help landlords tangibly improve their space and save on costs, Flageole notes.

And corporations may also choose the option to rent separate meeting or desk space from firms such as LiquidSpace just when needed rather than having it be part of the corporation's overall square metres of space, which adds to annual leasing expenses. But that goes both ways, and firms with excess space can rent it out for short periods of time over the Internet to offset costs.

While such short-term office rental initiatives are in relatively low use today, they could become more widespread as businesses seek cost efficiencies and become increasingly mobile, says Flageole. "From a business strategy perspective and looking at the office sector, we believe that listed companies will need to open up to new concepts to expand their potential tenant base," he adds.

To be sure, the shrinking need for physical space to work as a result of telecommuting, mobile computing and the like will, in the long run, have a negative effect on office space demand. This means investors will need to exercise greater selectivity over office investments by focusing their efforts on "the largest markets with a diverse tenant base," says Alice Breheny, global co-head of research with TIAA Henderson Real Estate. And future occupiers in the office sector are likely to be most attracted to renting space in technically advanced modern office buildings that provide the greatest flexibility for their needs, Breheny adds.

Staying competitive in the digital age will require landlords, tenants and developers to routinely assess and adapt to change as technological advancements continue to shape how people work and how organisations conduct business.

E-commerce, Alibaba and next-wave retail

When Alibaba's founder Jack Ma visited the United States from China in 1995, he was exposed to the Internet for the first time, and his resulting search for the country "China" left him with "No data found", which he realised meant nothing direct from China could be ordered online as it could from other Asian nations.

A few years later, Ma founded Alibaba — often described as a mix of eBay, Amazon and Google — and has now filed to list Alibaba on the New York Stock Exchange in what may possibly become the largest tech IPO ever, surpassing even Facebook's US$16 billion IPO in 2012. Here are some other items worth knowing about Alibaba and China's online marketplace:

- In 2012, two of Alibaba's portals transacted 1.1 trillion yuan (US$170 billion) in sales, more than competitors eBay and Amazon combined.
- Websites held by Alibaba Group account for more than 60 percent of the packages delivered in China.
- China had a first quarter 2014 year-over-year increase in online retail sales of 51.7 percent, according to the country's National Bureau of Statistics.

- Annual online sales in China are expected to reach US$650 billion by 2020, up from around US$190 billion in 2012, according to the McKinsey Global Institute.

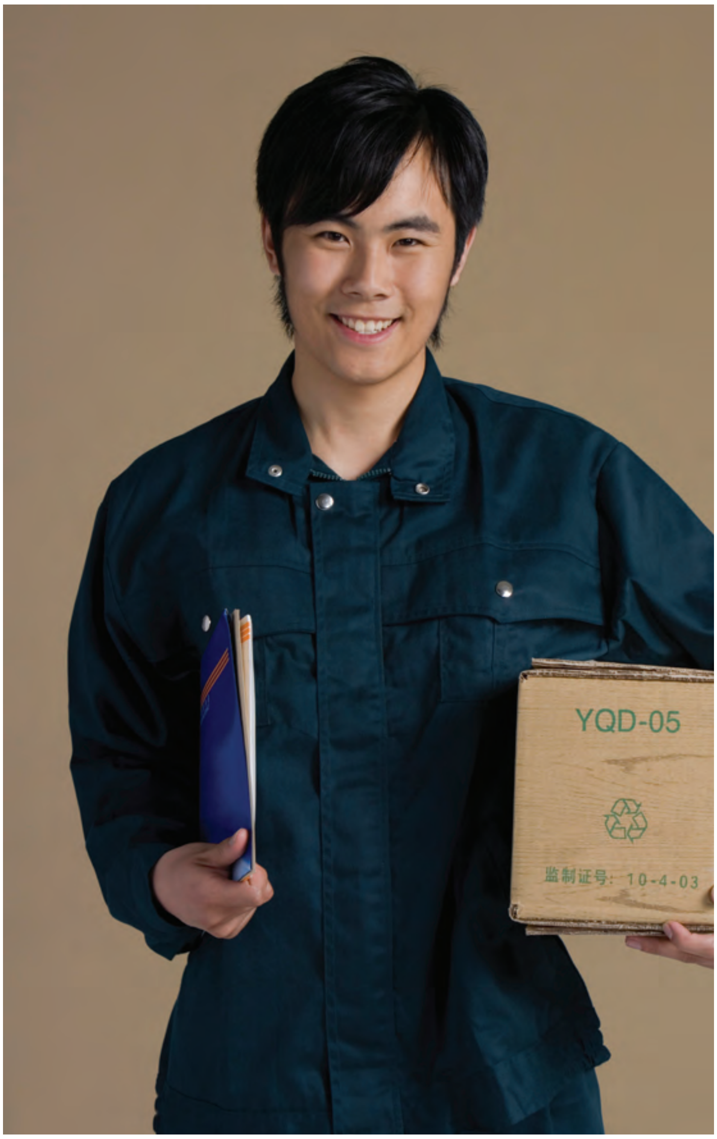
Does this mean Alibaba, Amazon and other online retailers are poised to take over the retail world, doing away with brick-and-mortar establishments once and for all? Hardly. But pressures to adapt will remain. While it is true that some physical retailers have struggled to keep foot traffic and stay competitive given the new cyber marketplace — and there is retail asset oversupply in parts of China — this is all part of the retail industry's evolution in a new digital age.

But there are pros and cons to e-commerce and online shopping for the retail industry that must be considered, suggests Stanley Ching, senior managing director and head of real estate group for CITIC Capital in Hong Kong. The good news, he says, is that e-commerce and online shopping will help increase the total retail sector pie in China, given there will be more channels for retailers to sell products not only to people that live in the area or region, but to sell brands online to people who otherwise would not have access to them. Additionally, e-commerce and online shopping can complement each other, meaning that brand awareness has the potential to increase and result in higher demand.

On the negative side, Ching cautions, e-commerce and online shopping are relatively unregulated in China, which will lead to increased disputes between retailers, vendors and consumers. And while the online shopping trend in China has been growing at a fast pace in recent years, the "infrastructure to support the sector is far from sufficient," Ching says. Finally, retailers and their brands could be negatively affected if they do not handle e-commerce and online shopping channels properly, which could especially be a problem for the many retailers in China new to using such channels.

And when it comes to brick-and-mortar establishments, "developers of new shopping centres have the opportunity to embrace multi-channel retailing — and should be investing in creating a true multi-channel experience," says TH Real Estate's Breheny.

While investors and listed firms owning retail assets will need to "proactively adapt to technology," they do not necessarily have to "revolutionise their operations dramatically," says Presima's Flageole. He notes successful malls globally have become "lifestyle destinations" in addition to being shopping centres. Some initiatives in these lifestyle destinations include higher-quality food and beverage options as well as large-scale entertainment events that have been organised by landlords, which gives potential customers added incentive to visit the mall.



Landlords (and retailers) can also be successful by incorporating new technologies in their space to complement the traditional retail experience, Flageole suggests, such as:

- Apps to promote retailers, which can advertise products and promotions in real time
- "Click and collect", which allows customers to order online with in-store pick-up or in-store returns
- Options for customers visiting the store to place orders online via a kiosk, phone or tablet

Australia-based Westfield Group, for example, introduced pick-up boxes in some of its malls for customers who have made online purchases. And in the firm's Westfield Sydney mall, the company is developing an app that will allow customers to order food online and pick it up from the mall's very popular and crowded food court.

Flageole notes that tech-embracing initiatives such as these "should ultimately contribute meaningfully to enhancing [mall performance]" but that landlords must support such initiatives for traditional stores to remain relevant.

Box it, ship it, get it to me now

If you take Asia's growing urbanisation and rising incomes into consideration, as well as the exponential increase in online sales, then logistics becomes the "missing piece of the puzzle for e-commerce companies to grow," according to a second quarter 2014 *Greater China Quarterly* report from Julius Baer Research. In addition to increased demand for industrial and logistics assets, the report highlights the following trends and potential for the sector in China:

- Current logistics systems are not efficient, and costs remain high as a percent of GDP.
- E-commerce will drive huge demand for logistics, but companies will need to invest and create strong delivery networks.
- Rural areas have tremendous value waiting to be unlocked, and e-commerce companies have invested in these areas as they realised the incremental value from these areas.
- With the popularity of smartphones, faster mobile Internet services and more efficient logistic networks, e-commerce could see growth in the coming years, particularly from mobile.

Importantly, even how companies set up their distribution centres is being influenced by consumers' desire for shorter and shorter delivery time, says Chris Caton, head of research with Prologis.

"The realities of transportation costs and rising service-level requirements create a need for companies to locate distribution centres and rapid fulfilment centres closer to end-consumers," Caton explains. By doing so, Caton says, firms are better able to balance faster times to market — primarily with next-day or same-day deliveries — with shorter inventory cycles and transportation costs.

And the need for distribution facilities closer to population centres and end-customers is also seeing a number of firms build modern logistics centres to replace some of their antiquated facilities, which are typically far away from population centres and "poorly configured for modern requirements, which emphasise throughput distribution over storage," Caton notes.

Macro fundamentals are relatively strong for the industrial and logistics sector in the Asia Pacific region, which bodes well for demand, according to a first quarter 2014 *MarketView* report from CBRE Global Research and Consulting. These fundamentals include increased industrial production, robust consumer demand and an improved trade outlook (aided by growth in organised retail, e-commerce and third-party logistics expansion and relocation to and within Asia).

The future is now

What holds true for members of the real estate investment community is the same for business leaders in general: They must work now to understand and determine how their competitive advantage, which informs business strategy, might diminish or be enhanced in the coming decade by various emerging technologies, states McKinsey Global Institute's May 2014 report *Disruptive technologies: Advances that will transform life, business and the global economy.*

For institutional investors, says Presima's Flageole, technological advances may create an opportunity for them to gradually access new real estate sectors and income-producing rental properties, such as in the wireless communications sector. This has already been seen in the data centre sector, most notably in the United States, but recently in Japan with the February 2014 IPO and listing of Hulic REIT on the Tokyo Stock Exchange.

So will institutional-grade real estate assets be bought and sold in the future with Bitcoin, or will goods be beamed into our homes from a Star Trek–like transporter? Probably not any time soon. In looking to the future of the real estate industry, we have to take into account what we know about the fundamentals of human behaviour within the confines of economic markets: people are social creatures and like to own things, typically need to work to support themselves and their families, and they need to live somewhere while doing so. These simple aspects of human behaviour in a financially-driven world mean brick-and-mortar real estate assets are here to stay.

But this digital world we live in is revealing vulnerabilities almost as fast as the benefits we have integrated into our daily existence and have come to rely on. Real estate investors will need to remain vigilant as they develop business strategies that take into account what new technologies can do for their investments in the short and long run. ❖

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