Successful M&A: capturing value through real estate
Mergers & acquisitions are on the rise

Mergers and Acquisitions activity is currently at record levels. Worldwide deal-making is up 32% from 2014; with 2015 witnessing the first back-to-back $1 trillion+ quarters since 2000 globally. In Europe, healthy corporate balance sheets, renewed confidence and attractive financing conditions have all boosted deal activity. From mega-deals to smaller acquisitions, companies are once again exploring the M&A market as a way to secure a competitive edge.

The number of cross-border deals is also on the rise, increasing deal complexity and challenging companies to find new ways to drive greater synergy and value. Rising shareholder activism and ever-increasing transparency is putting a brighter spotlight on M&A strategy than ever before.

Key figures:

- Sharp increase recorded in M&A activity in the EMEA region (Europe, Middle East, Africa)
- $350 billion in the first half of 2015 compared with the first half of 2014
- Surge in mega deals (exceeding $5 billion): up 47% in 1 year
- Top 5 sectors: Energy, Health, Extractive Industries, Telecoms, Manufacturing Industry
- 43% increase in pending transactions compared with the previous year

Sources: JLL, Thomson Reuters and Intralinks

How do you use real estate to maximise value in the M&A process?

Our conviction, and that of a wide range of companies which took part in our study, is that real estate, when skilfully integrated and managed, can be instrumental in maximising the value from M&A at a number of critical points in the transaction process — from pre-announcement to integration. It is also equivalently clear that insufficient attention to real estate can carry great risks. This report features research and survey insight from over 50 companies exploring M&A and the role real estate plays in successful transactions.

76% of companies involved in a merger or acquisition over the past five years consider real estate an important or critical factor of success
Executive summary

Our research revealed that real estate, when skilfully used, can create value for companies in four major ways throughout the M&A lifecycle. There is, however, an additional critical factor which underpins value in each area.

1. Mitigate risks

The timely provision of comprehensive data and insight on real estate portfolios in the due diligence phase means a more robust business case and better assessment of the financial, operational and business continuity risks associated within the M&A process.

2. Optimise costs

Real estate is often the second-biggest cost on a corporate balance sheet. From portfolio benchmarking to more accurate valuation and forecasting, there is a range of tools available which help companies measure, anticipate and avoid unnecessary costs within the M&A process, without impacting deal timelines.

3. Accelerate operational strategy

Effective footprint optimisation and a fully aligned real estate strategy can greatly enhance and reinforce operational objectives. For instance, by designing a new real estate master plan aimed at rethinking the company’s real estate footprint, consolidation opportunities can be identified, while operational efficiency, productivity and performance can all be increased.

4. Ensure successful integration

Real estate can play a crucial role in facilitating business continuity and successful integration. Early integration of real estate into the M&A process can help companies achieve a smoother path to a new corporate identity and culture. Well-designed real estate solutions can improve the integration of separate entities.

Accurate Data + Insight underpin all the risk, cost, operational and integration benefits we identify in this report. Optimal business decisions and outcomes require transparency, and real estate data is no exception.
Mitigate risks

In many cases, real estate is not sufficiently integrated in the due diligence phase.

In the due diligence phase, high-quality real estate information makes it possible to anticipate the operational, financial and business continuity risks associated with real estate.

Timely integration of real estate data and insight can influence negotiations concerning the acquisition price.

M&A survey: Key statistics

82% confirmed that their real estate carried business risks in the M&A process

Yet .... 21% having undergone an M&A did not involve the real estate team in the transaction

And in the future... respondents expect earlier integration of real estate

55% Before the official external announcement

29% After the official external announcement and before the closing of the transaction or on “day 1”

16% During the integration phase
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In the past, real estate was not factored into the deal decision, and the company took on additional risk and cost. In some cases, we discovered we had acquired more sites than estimated, and that real estate values recorded on the balance sheet were twice market prices.

Real Estate Manager of a leading household appliance and medical equipment group

By nature, M&A transactions carry risks, including operational, financial, legal, and real estate risks. They constitute a challenge to business continuity. To best assess and address those risks, companies invariably conduct a detailed due diligence review, which enables them to make all the verifications they deem necessary before completing a transaction.

At this stage, many companies do not include a real estate component in their analysis. However, a growing number of companies are becoming exceptions to this trend. Their due diligence reviews cover real estate, along with financial, legal, operational, and HR aspects. The real estate aspect can go as far as to influence negotiations concerning the deal value and even—in cases where the real estate is particularly strategic, as in the retail sector—be instrumental in the choice of the target.

Integrating real estate into the due diligence process helps identify and quantify the risks associated with the company’s real estate commitments.

Real estate due diligence rests on knowledge of the portfolios of the acquiring company and target company, including:

- The amount of rent and associated charges payable for leased buildings; indexations, late payments, and the transferability of lease;
- The value of the sites owned recorded on the company’s balance sheet, sometimes out of sync with actual market prices;
- The duration and flexibility of lease commitments and site-control issues stemming from the contractual relations between the acquired company and its lessor—in particular the exit costs associated with the early vacation of certain buildings;
- Geographic footprint, including portfolio size and annual Opex impact;
- Environmental due diligence and analysis of any risks related to contamination;
- Review of contractual agreements with outsourced service providers and third parties;
- The state of the premises and capital expenditure that may be required to upgrade them to the acquiring company’s standards, to promote integration and retain talent; and
- Discrepancies between available premises and the needs of the operational teams following the transaction.

Having access to the real estate data ahead of the deal is essential. It can have a direct impact on the acquisition price and can even be a reason to abort the deal if major risks are identified.

Purchasing Director of a leading semiconductor group

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Real Estate Manager of a leading household appliance and medical equipment group
Optimise costs

Cost optimisation can be accomplished through numerous methods: rationalising portfolio size and sites, consolidation and sale of certain assets, benchmarking and leveraging increased bargaining power.

M&A transactions provide a perfect opportunity to restructure the organisation and rationalise real estate expenses.

The restructuring of the portfolio may involve the (re)defining of a real estate master plan in order to set a target solution and a road map to achieve it.

Real estate cost optimisation can be a crucial tool for companies to achieve the required synergy targets and return on investment from an M&A transaction.

M&A survey: Key statistics

Of companies surveyed state that rationalising real estate expenses is one of the two areas in which the real estate team can provide the most value.
Real estate expenses are often the second-biggest expense item on the balance sheet, after people. Within the scope of a merger or acquisition, real estate can thus constitute an invaluable opportunity. M&A transactions provide the opportunity to overhaul the organisation and rationalise real estate expenses. Generally the due diligence phase presents the best opportunity for early opportunity identification, with implementation phased from day one.

One of the most important steps for identifying cost-optimisation opportunities is a comprehensive portfolio assessment of real estate assets and commitments. Ideally this should begin during the due diligence phase. Among other things, the assessment should explore cost-saving opportunities, including:

- Passing rent versus market rent
- Service charge benchmark
- Facilities management cost review (cleaning, catering, maintenance, etc.)
- Utilities and energy cost review
- Total Opex analysis
- Break options and early vacation analysis
- Lease/sublease disposal review
- (Co)location options for business units and incoming employees
- Workplace optimisation and/or space reduction

Once a full and comprehensive analysis has been undertaken, a portfolio restructuring strategy and comprehensive real estate master plan can be put in place to help deliver synergy targets.

All of our acquisitions gave rise to real estate decisions: 75% of them involved lease rationalisation plans, 10-15% involved sales while the rest were logistics decisions.

Global Real Estate Manager of a leading household appliance group
Accelerate operational strategy

A well-aligned real estate strategy can accelerate operational objectives in an M&A transaction. This requires careful planning, alignment and constant review from due diligence to business as usual.

Enterprise footprint-optimisation processes can improve operational efficiency, productivity and business performance through network planning, location analysis and realising consolidation opportunities.

Location strategy, real estate and workplace decisions can have a tangible impact on strategic objectives, such as talent retention, brand objectives or even business continuity.

M&A survey: Key statistics

of the companies surveyed made decisions concerning the optimisation of their real estate portfolio following their M&A operation

Strategic alignment and enterprise footprint optimisation

Real estate can help accelerate the operational objectives in an M&A transaction in a number of ways. Close alignment between real estate and those functions determining and executing the M&A strategy is an essential pre-requisite to ensure value is achieved throughout the process.

More specifically, a process of enterprise footprint optimisation can help ensure that the locational and business network of an organisation is fit for purpose and maximising performance objectives in a newly merged entity.

Enterprise footprint optimisation is an ongoing process, and there are a number of important considerations.
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Align real estate with business strategy — Is your real estate strategy supporting the strategic M&A objectives?

Location strategy and network — What is the ideal location for R&D, manufacturing or regional office hubs? (e.g., how does the new organisation want to engineer its sales force?)

Supply and demand for new entity — What is the current supply of and demand for real estate in the new entity?

Current state vs future state — Is the current footprint fit for purpose? How will this change through the process of the integration and medium-term growth?

Off shore and onshore — What is the optimal mix of offshore and onshore facilities for the new entity?

Have lower cost onshore or offshore hubs been explored to drive efficiency? Shared services — Would shared service centres drive additional value for the new entity?

By allowing the merging of the head offices, the real estate assets meet our need to rapidly integrate the support services teams. And they make it possible to finalise the acquisition project.

Real estate manager of leading chemical industry group

M&A is often used as an opportunity to clean up the real estate portfolio. Identify opportunities, consolidate, deliver savings quickly — then take a restructuring charge.

Global head of real estate, leading lifesciences company
Ensure successful integration

Real estate can provide management with an important opportunity to establish a new brand and corporate identity.

The new work environment can be transformed into a tool to promote integration, talent retention and collaboration.

Effective real estate and facility management is essential to ensure business continuity, while the integration phase provides the opportunity to capture the synergies highlighted during due diligence.

M&A survey: Key statistics

Following the M&A completion, the work environment is clearly perceived as a lever to be activated.

50% of surveyed companies stated that they had made decisions concerning workplace strategy, such as defining new layout guidelines to promote the adoption of new working models, during integration.

When interrogated on the two areas in which real estate creates the most value...

53% cited the management of the real estate portfolio to support synergies, the new culture and the new brand.

However, only 8% of companies cited the impact of real estate on talent retention.
Successful M&A: capturing value through real estate

Our survey revealed that, in the face of difficulties, such as governance problems, cultural differences, organisational divergences and failed synergies, integration can be accelerated by a company’s proper use of its office space combined with a well-balanced programme to manage the change. Conversely, a disparate, segregated work environment can inhibit collaboration and productivity — two essential factors in an integration phase where two corporate cultures and two organisations are learning to work together.

The speed of integration post-merger can be a critical driver of deal value – real estate can definitely facilitate this.

Head of global real estate in a leading pharmaceutical group

Effective integration is critical for creating lasting value in M&A, and real estate can create the physical stage for that to occur.

According to PWC, “value is created during the post-merger period” and with analysts tending to base their assessments on the acquiring company’s stock market value after a period of 24 months, the closing of the transaction is thus only the beginning of the challenge that the consolidated company has set itself.

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Real estate is a powerful tool for establishing corporate identity and retaining talent

Real estate provides the opportunity to give concrete expression to the company’s new identity. It enables the executive management to display its answers to affiliation issues in the organisation’s premises.

- How will the acquiring company and the target be combined?
- Will the acquired company retain its specific identity or will it be fully integrated?

In our integration plans, we tried to mix the teams of both entities as much as possible. It was a delicate matter: we had decided to merge the entire workforce of the two entities in the premises of the acquired company. We had to ensure that everyone felt at home.

Merger Project Manager, Medical Services Director of a leading pharmaceutical group

Talent retention is usually an important focus in the integration phase of an M&A transaction. The location and workplace can have an enormous psychological impact on the morale of the workforce. Workplace design can also send strong messages to staff. For example, by bringing together the members of the new organisation’s executive management in the same space, irrespective of their prior ties to either of the companies, clear messages can be delivered regarding the new organisational structure.

The workplace has the potential to be a powerful instrument of integration for the new organisation. Through the layout of the work spaces and (co)location of teams and departments, the work environment becomes a theatre where the new management conveys its values and convictions. The offices thus let employees “see” and “experience” the company’s new identity.

A process of prioritisation is an essential part of delivering real estate value throughout the M&A lifecycle. In the initial phases of integration, strategic locations will likely be the primary focus, with a stringent focus on capital expenditure to ensure the real estate strategy complements financial objectives.

Our challenge today is to develop a feeling of belonging, cohesion and team spirit. Even though the activities of the company we are acquiring are independent from ours, we feel it is essential to share common, unifying values. Our offices must promote adherence to our core values.

Real Estate Manager of a leading chemical industry group

Ultimately, the integration phase is where many of the identified real estate synergies can be realised.

This begins with the basics of effective facility management (catering, cleaning, parking, security, etc.) minimizing disruption and ensuring business continuity. But as we have seen, the impact of real estate in the integration phase can extend far beyond business continuity. From talent retention to unlocking cost savings, the integration phase is where strategies for efficiency, consolidation and value capture can be executed.

M&A real estate flow diagram: major activities
Turning your real estate into a factor of success

1 Start thinking about real estate as early as possible.

As we have seen, too few companies start their real estate analysis before the closing of the transaction. Too often, the real estate team is approached only once due diligence has been conducted — and once the purchasing price has been agreed. However, the companies, which include real estate analysis in their due diligence phase report a real gain in terms of added value.

"Having real estate info ahead of time is critical. It can have a direct impact on purchase prices, and may even break the deal if significant enough."

Real Estate Manager of a leading IT services and consulting group

2 Manage confidentiality requirements.

This is undeniably one of the challenges of an M&A project. Very often, the acquiring company has a hard time accessing the target company’s real estate information. Top management does not want privileged information disclosed before the agreement is signed. Independently from the acquisition context, real estate data is not always recorded in a stringent manner. However, the analysis of real estate scenarios and compliance with confidentiality obligations are not incompatible. There are a number of models and processes which can be adhered to which allow comprehensive data and insight to be provided pre-merger while meeting stringent confidentiality requirements.

"The main difficulty in the due diligence phase is that the review has to be done on paper: because of anti-trust laws, we are rarely allowed to go on site."

Real Estate Manager of a leading IT services and consulting group
At the start, our management team was not convinced that the real estate department should participate in the due diligence phase. They feared that this would slow down the acquisition process and were wary of the introduction of technical experts. It was thus essential for the real estate team to confirm that we would comply with their deadline and that we would adapt to business requirements.

Real Estate Manager of a leading household appliance and medical equipment group

3 Speed is crucial to maximise value.

Speed is absolutely critical to success in any M&A transaction. Any real estate analysis conducted during the due diligence phase must be conducted over a very short time, and this cadence usually needs to be maintained during implementation. The challenge consists in reconciling the need for rapid action on the part of the company during this unsettled period, and the long cycles applicable to real estate — due in particular to lease commitment, research and construction lead times, etc. To address this challenge, the market expertise and services of real estate specialists in the M&A process becomes a real asset.

4 Build a real estate solution fully aligned with the acquisition strategy and objectives.

This strategic alignment will need to be based on thorough knowledge of the company’s workings and strategy. The good relationship established between the real estate department and the decision-makers is therefore a key factor of success, which will ensure the design of a tailor-made solution covering all merger requirements. This process of alignment and relationship management can take many years to develop, but is perhaps the greatest mechanism for ensuring the value of real estate is fully realised in the transaction process.

If you don’t have good knowledge of the company’s business and you only present yourself as an expert in real estate issues, you are seen as a cost play. Talking the same language as the business, and understanding the strategy and the needs of the operational teams is essential. This relationship must be nourished continuously, on a day-to-day basis.

Real Estate Manager of a leading household appliance and medical equipment group
In an organisational project as complex as a merger or acquisition — combining functions and objectives across the entire corporate organisation — it seems obvious that the companies that are able to connect their data and combine the expertise of their various business functions will have more chances of success. Integrating real estate workstream alongside strategy, HR, IT and the many other workstreams is the best guarantee of success. The amount of time and resources required to deliver a successful M&A process can be huge. Planning in advance and creating robust processes and appropriate resourcing models are also essential. The outcome will be the joint construction of a new work environment which will act as the seedbed for value-creation in the combined enterprise.

"The human dimension must never be dissociated from the real estate aspect. The real estate consultant has great value, as he/she can help the company build a work environment which meets both financial and human requirements."

Merger Project Manager, Medical Services Director of a leading pharmaceutical group
Are you maximising the value of real estate in the M&A process?

Each project is unique

The wealth of testimonials collected enables us to assert that no standardised solution can apply to the variety of situations and challenges encountered in M&A transactions.

The chosen real estate strategy will only prove relevant if it takes account of the specifics of the merger context: business segment, sizes of the acquiring company and target and nature of the operation — merger, acquisition, joint-venture, company purchase, sale, carve-out, etc. It will also need to be suited to the size and composition of each company’s real estate portfolio, as well as its business objectives. However, there is much that can be done to prepare the ground for successful integration of real estate in the M&A process.

Preparation and proactivity will deliver results

Is M&A activity on the agenda for your company?

Instead of waiting to act, be proactive.

• Establish M&A management processes aimed at mobilising the different stakeholders;
• Create an M&A playbook: a set of steps that can be tailored to each unique transaction;
• Make your real estate more flexible — for example, by aligning your leases or by designing easily modifiable layouts promoting synergies — in order to give your business the required agility and enable it to easily integrate new employees; and
• Nurture relationships of partnership and transparency with all business functions and services, as well as with the organisation’s highest levels.

“Mergers and acquisitions are now part of companies daily existence. You don’t have time to create process on the run, large opportunities and millions of dollars of benefit can be lost.”

Head of global real estate in a leading pharmaceutical group
Methodology

To address this issue, we sought the views of a range of experts in different sectors and companies, as well as drawing on our own international experts advising companies in the M&A process:

1. A quantitative approach in order to obtain appraisal data.

An online survey conducted in July-August 2015 with forty international companies established in Europe and involved in merger and acquisition operations over the past 5 years. Most of the respondents were from real estate departments, financial departments, HR departments or operational departments.

2. A qualitative approach.

A qualitative approach, using one-hour interviews conducted with fifty companies with M&A projects across Europe, including PHILIPS, ARMONIA, DIA, DUPONT DE NEMOURS, MSD, TOUS and many others.