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Presenter:

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Title: Industry Consolidation – An Era of Employment Uncertainty

Theme: Employment Impact: Predicting the Unpredictable

Subject:

Many real estate organizations and building owners are frustrated in today's marketplace with respect to the difficulty in finding service orientated and experienced property managers, building operators and superintendents. And if they find them, their next challenge is how to retain them.

This presentation will examine some of the key trends affecting building management staff and professionals including:

- 1) Revaluation of the property manager through job enrichment;
- 2) Motivate by making your values mean something;
- 3) Compensating Performance by offering clarity, simplicity and execution;
- 4) Retaining talent (determinant factors for staying or leaving.);
- 5) Recruiting talent (when and how, secrets of a corporate headhunter);
- 6) Implications of the future labor market (more than the building's life cycle should be extended);
- 7) Effect of mergers on staffing (an age of uncertainty);
- 8) Warehousing knowledge that's transient (managing the knowledge gap between senior and junior employees);
- 9) Career Management (finding one's niche in an oligarchic industry);

Opening Preamble:

This morning, I want to speak about the present and future – perhaps offer you some assurance that career opportunities within the Canadian real estate industry are bright. There really isn't any need to speak about the past - all of you know where you've been, most of you know where you are, and some of you know where you're going. One simply needs to step back from the industry, and take a good look – it's a matter of perspective.

I've been involved in real estate executive search since the mid-80's – and prior to this, I worked in real estate development in Canada and property investment overseas. I'm perhaps one of a few headhunters' specializing in real estate that has experienced all of the property cycles. Unquestionably, like you, I understand the concept of living with uncertainty.

We're in a unique position to observe the changing macro trends and oncoming challenges facing the Canadian real estate industry as a whole. We have developed insights essential to understanding competing businesses, their organizational culture, needs and weaknesses. This familiarity with industry trends, is resultant from a consultative relationship with clients, but is due as well to the summative information we acquire through thorough and candid interviews.

With the ongoing mergers and acquisitions – all indication would suggest, we are an industry in contraction. Employment retention levels are currently stable, with large firms experiencing only a marginal or selective level of churn within their ranks. Under normal circumstances, employee retention is an indicator of corporate stability, and a measurement for determining a firm's underlying long-term corporate value. However this period of stability is transitory; and reflects the perceived capital strength and relative employment security offered by these firms.

Upper middle and senior management have suffered the greatest in terms of becoming redundant through this consolidation. By and large, job security is primarily at the line level – the closer you are to the bricks and mortar – the better off you are.

Employee retention over the medium to long-term will be less stable, as I predict there will be a shortage of qualified real estate professionals. These predicted shortages will not be measured in **terms of a shortage of human assets**, but rather in the diminishment of knowledge assets.

The brochure, introducing this session stated, "real estate organizations and building owners are frustrated in today's marketplace with respect to the difficulty in finding service orientated and experienced property managers, building operators and superintendents. And if they find them, their next challenge is how to retain them." My friends, if you think it's bad now – I'm here to tell you that what you're experiencing now is merely the tip of the iceberg.

WITHIN five years we will undergo a shortage of trained staff and management talent. Our most seasoned and socially networked employees will begin to gear-back or take early retirement.

IT IS NOT MY INTENTION – to stand up here and present myself as some sort of Pollyanna - or tell you the glass is half empty, the sky is falling, or that the industry has reached a stage of climax and no further opportunities exist.

QUITE THE CONTRARY – **real estate is cyclical and dynamic**, the business paradigms, which exist today, may not necessarily exist tomorrow. To understand this assertion, one only needs to review recent business history and list the iconic names that no longer exist, apart from a shell company on a receiver's shelf.

The Canadian commercial real estate industry may best be described as a **complex adaptive system** – complex adaptive systems can appear to move to the **brink of chaos** before new patterns emerge and new forms of organizations take shape.

It has become an industry, which is both oligarchic in one massive sector with a potential to control for supply and face rates – and yet - we have more public real estate entities today, than we did during the heady days of the late-eighties.

Even as we witness the merging of traditional firms, and the acquisition of trophy portfolios and assets – **new companies are emerging** – they're emerging as unique, agile and focused forces – this is their competitive advantage.

The growth of REIT's, the creation of small cap development and acquisition companies, the emergence of fee based corporate services companies – all are clear examples of our industry's adaptability and capability to generate new methods of operating.

HOW CAN THIS BE?

The answer lies within the ethos of the industry, the deal driven personality of industry executives, and the industry's unparalleled capability to leverage capital to create value.

The downsizing of merged and acquired companies has significantly impacted the management levels, however displaced management is fertile ground for entrepreneurs and financial backers. There are many examples of entrepreneurial personalities resurrecting themselves at all levels of the spectrum – at the international level – Paul Reichman assembled a capital pool to buy back Canary Warf; nationally - Jon Love and Stuart Lazier left their respective companies and within mere months - launched a multi-million dollar acquisition fund – and more recently, Bill Minnis with a core of his former pension fund advisory team announced the creation of real estate money management firm.

This sub-strata group of companies operates below the radar of the major players – **they are nimble – and quick – and they're competing for talent** within an industry that has spent the last thirteen years draining the talent pool.

What are the contributing causes for this talent shortage?

The answer is simple; the present situation is due to our ten-year inaction to:

1. Educate internally,
2. Support external educational institutions adequately,
3. Value and mentor the talent we have,
4. Adequately pursue a coordinated on-campus recruitment program.

These are the contributing causes, however the future cause is daunting – a rocky shoal, and more difficult to navigate around – it's "**DEMOGRAPHICS.**" Add labor shortage to talent shortage – and I suspect the employers among you will get a migraine – from my perspective – I'll get to raise my fees!

LET'S CONDUCT AN EXPERIMENT – would all of you indulge me for a moment and stand up.

Now, assuming your RRSP didn't get hammered in the markets – those of you, planning to gear back or retire by 2008 – sit down.

By 2013 – sit down.

By 2018 – To those whom are sitting, take a hard look at the people that are standing – for they and their peers are the future of the industry – the challenge is to ensure that you impart your knowledge upon them.

If the industry is to close the knowledge gap between young and old, **companies must take an active part in developing training programs based on mentorship and collaborative systems.** Such systems are designed to archive the expert knowledge, which resides within each firm.

Knowledgeable Labor Supply – Competing Demand

This knowledge/labor shortage is not exclusive to the real estate industry, it's systemic, and will include both upward pressure on both employee compensation (to attract talent) and taxes (to support a politically sophisticated and self indulgent gray market) on corporate and individual earnings.

In 15 to 20 years – the ratio of workers to retirees will be approximately 3.7 to 1 – in 30 years, 2.7 to 1. The tax implications are astounding – imagine so few workers supporting one retiree – it is simply untenable.

We are already seeing indications of labor shortage impact – consider our federal government – that bastion of leadership – where self-interest trumps integrity, historical alliances and the public good – during the next decade, a significant portion of the public service will retire.

Rather than finding efficiencies in process or forcing the assessment of a programs value through legislated sunset clauses, and thereby reallocate human resources accordingly – our government responds to this crisis by hiring seven thousand new employees annually just to stay even. The stated hope is that existing employees will rub their experience and knowledge off on the new employees prior to the full impact of the baby boom bust. **It's kind of a “Hobson by the water cooler” approach to training.**

The problem is universal - throughout our public and private institutions – and at both the municipal and provincial levels of government. For instance, New Brunswick projects some of its government ministries will lose up to 50% of its managers over the next seven years.

Consider Canada's Schedule A banks and their efforts to merge – they have very little choice but to merge – domestically, short of fees, they've reached their limits to growth, and are cannibalizing market share. Internationally - global competitors dwarf them.

To be competitive is clearly, the primary force driving the banks to merge; however, banking is a knowledge industry with a significant knowledge based workforce. Even with technological efficiencies, the banks were quick to recognize the approaching knowledge gap within the financial services sector is a market force of its own, equally driving their need to merge.

Imagine the impact these mergers will have on office space both directly and indirectly. It is significant, when one considers how many professional services firms and suppliers on the losing side of these mergers will be forced to downsize or merge.

So you see my friends, the watchword in our economy is “demographics” – for everything in your future – **all that you hold important** – family – career – lifestyle – healthcare – wealth – governance - will be influenced by this single fundamental and encroaching reality.

Does the property manager feel valued?

In an industry with oligarchic overtones in some sectors, one should not assume the lack of turnover is necessarily indicative of a satisfied employee base. Subject to the financial strength of their firm, people are staying put **hoping for promotions but are settling for lateral enrichment.** For the most part, companies are not providing this

sought after lateral enrichment, and in some instances, we've observed a trend towards functional diminishment.

For example, consider the office property manager responsible for an urban or edge city asset greater than or equal to 700KK sq. ft. – **he/she has their CPM or RPA** – this experienced manager represents the top tier of your property management class and represents a **wealth of experience, industry knowledge and vocational commitment**. Yet - many in this function feel diminished in their scope of responsibilities, relative to what they had some years ago.

I recognize that I'm generalizing, for certain company's are attempting to enrich the scope of the senior property managers duties - requiring them to take greater ownership of their budgets, assuming roles of construction coordination, procurement management and innovate cost efficiencies.

However, coupled with this desire for managers to take a more integral role in suggesting or implementing value adding strategies to their portfolio, is the **need for a strong corporate commitment on education and mentorship**. The folly in this strategy is to enrich the scope of a position without reciprocal action on increasing the employee's capacity to meet the raised benchmarks of performance.

Today – it's hard to draw a bead – each company has a different approach – some offer their property managers a great deal of leeway in the management of their properties, while others won't give an RPA or a CPM overseeing 2MM sq. ft. or more - the discretion to spend \$500.00 outside of budget.

In a letter to senior executives within the industry, I expressed concern about the knowledge gap we would be facing by writing the following, *"I believe the success of 'brick's and mortar' in the twenty first century will be less contingent on 'location,' and more so on the performance and competencies of the people that develop, own and manage them. The essential assets and strengths of a property reside in the people that nurture its life cycle; ergo the essential assets and strengths of a property portfolio will be determined by the ability to integrate best practices and processes throughout the organization."*

Executive response varied in tone, ranging from the supportive to pleasantly dismissive. Representative of one extreme, was a senior asset manager, whom was strictly interested in **"today's value,"** and didn't subscribe to the belief that operational staff impacted values or building life cycle at all; while another executive was quite energetic in describing his efforts to foster a long term value-based culture that welcomes initiative from the rank and file.

The Canadian commercial real estate industry is framed around an austerity business culture, a necessary survival strategy in the early to mid-nineties but a disadvantage to the industry today. **In my opinion, due to this austerity culture, a**

number of owners and asset manager's have lost their way with respect to the valuation of their people.

Insulating your firm from this approaching knowledge shortage?

The medium-term human resource challenge for CEO's will be developing policies which address career development aspirations of the company's existing workforce and foster an organizational environment which will attract future talent.

Improved information management technology may mitigate workforce supply pressures by increasing individual productivity, however the most effective means for alleviating this approaching pressure is to extend the employee's life cycle through qualitative retention measures. The short-term solution is to delay the attrition by revaluing the role and scope of your key employee's contributions.

The industry is concerned about the state of skills development, however concern doesn't necessarily translate into action. Twelve years of under-funding skills development compounded by a net loss of talent and limited success attracting new recruits from post secondary and graduate schools over the same period of time leads to one conclusion – our second string has limited depth to replace what we'll eventually lose.

However, I believe this second-string weakness can easily be rectified through implementation of a variety of external and internal employee development strategies – the key is to subtly shift the culture of the firm to one that emphasizes learning, knowledge management and mentorship.

Cost effective technologies and strategies exist today, that allow companies to deliver credible academic and internal training programs to their staff. This can be achieved in unison with a program for capturing the wealth of knowledge that flows in and out of your organizations on a daily basis.

Clearly - the motivation to implement these strategies requires a champion in the executive suite.

Motivate by making your values mean something!

Ladies and Gentlemen: the secret to attracting quality staff and retaining good people is to **live your "core values"**, to **have a "core purpose,"** and to make them part of it.

Last month, I interviewed a highly competent and committed accredited property manager that had been laid off – **he wasn't laid off for cause** – he was laid off because they could replace him for twenty thousand dollars less.

Two months ago, I counseled a manager with exceptional depth and commitment to the industry that wanted to enroll in an executive MBA, she needed every second Friday off and a week of classes per annum over a two year timeline. She also needed financial assistance. The company responded by offering to subsidize a small portion of the financial cost, however she was no longer eligible for bonus – she must use her holidays for the week in class – **and oh yes** – she has to sign a five year employment contract with no steps in pay guaranteed.

Now I ask you – Ladies and Gentleman – have you ever heard of anything so absurd?

What are the values by which these companies operate – what are the essential and enduring tenets of their organization – that which is unalterable even if it becomes a competitive disadvantage – it's certainly not their people – I leave it up to you to define what these companies stand for.

A “core purpose” may shift with market realities, but a value should be unshakeable. Here is an example of a “core value” and a “core purpose.”

On 9 11, Cantor Fitzgerald lost in the blink of an eye – two thirds of its staff – I don't know what their core values were prior to 9 11; – however today - **one core value** that provides the glue which holds this company together, which **defines what they stand for**, - is “to care for the families of their fallen friends.” Cantor's “**Core Purpose**” is to return to the volumes of pre-911business. They've succeeded in both.

Is tenant service a core value in your organization? – Ask your employer or the asset manager responsible for your portfolio this question – “If tenant service becomes a competitive disadvantage, should we start cutting back?” If “cutting back” is their answer, then “tenant service” was never truly a corporate value in the first place.

People will come – and they will go, but where a company has a strong commitment to core values and purpose, I'll submit this company will get full measure of their employee's worth.

And why?

Because their **uncertainty will evaporate** - through the company's “Core values” they know who they are – and through “Core Purpose” they know where they're going – What can be more certain than that?

How should a firm maintain a supply of talent?

Poaching talent is always a time-honored tactical and strategic option, however job enrichment and cross training remains a critical means for retaining and attracting star performers.

The **greatest challenge for an executive search professional** is finding people that are able to recognize opportunity, to be able to visualize value where others cannot. Highly motivated people, with strong intuitive skills, who are able to conceptually perceive the “whole” and lead people to perform – these are the 20% that out perform the 80% regardless of the industry. To fly in the face of the behaviorists, these qualities are innate and are rarely learned after adolescence - **no matter how many** remedial Executive MBA courses you put the manager through.

When hiring a junior to intermediate employee, we should be more accommodating in our need for experience. Experience can be relative. There are plenty of people walking around with ten years of experience – however the problem is, once you interview them – you discover they have one year of experience – TEN TIMES.

Ask yourself, if the position really needs four years of experience? - Or is this a stipulation designed to avoid processing a voluminous response from personnel agencies or job board? When I assess a person abilities for a junior or intermediate position, it's not a question of judging them for who they are, but rather for “what they will become.”

Judging a manager is an exercise of distinguishing between their knowledge and skill. Knowledge is an amalgam of experience and technical competence and can be learned. Quite often, individuals are promoted too quickly to positions of responsibility over staff but lack the primary management attribute – interpersonal skills either within his or her business unit or at the client level. The industry is rife with highly technical managers that have no business managing staff until they've addressed their interpersonal weaknesses.

If you are **planning for succession** at your most senior strategic levels, then you need to determine the quality of your staff in the context of these innate qualities, however if succession planning for positions where experience, technical and interpersonal skills are sufficient then management should implement a policy of development through courses, mentoring and coaching.

There is more to job enrichment than upgrading the scope or raising management's expectations for a given function. You can enrich an employee's position by elevating their importance and recognize the value of their inherent knowledge by giving them responsibility for mentoring staff or acting as an expert resource.

Each person is different. It's imperative for a company to **understand which drivers' impact employee performance, retention and satisfaction**, as this measurement is a strategic tool in the overall human resource and skills development planning process. This can be done through the development of a matrix which gauges employees overall sense of job satisfaction. In such a study, you will often find that employees rank career and personal development higher in importance than

compensation. Understanding where employees measure their personal rewards or benefits of work, allow our clients to be creative in meeting employee needs.

At Rutherford International, our matrix is an amalgam of features, which include direct financial (pay), indirect financial (benefits), work content (the work itself), career (long term opportunity for development and advancement) and affiliation (feeling of belonging).

“Affiliation” (feeling of belonging) is probably the least understood feature our matrix, and yet creative management strategies that address this feature can be both powerful employee motivators and provide significant impact on adding to shareholder value. Employees with a strong sense of affiliation to their firm – **DON'T LEAVE**.

Tenets For Performance Compensation

I don't wish to convey the impression that compensation doesn't play a critical role in an employee's happiness. After all, this is the real estate industry, an industry with the highest per capita ratio of Type A personalities.

The concept of pay for performance is widely accepted in the real estate community, however **the link between incentive pay and performance is weak** and not necessarily connected to measurements reflecting long-term shareholder value creation.

With the consolidation of ownership, large companies have developed compensation philosophies and strategies for their front-line managers and staff, which may be cumbersome relative to more nimble compensation architectures at smaller competitors. This is a distinct competitive disadvantage, which more structured firms are attempting to address through the inclusion of variable pay programs based on performance. In a variety of instances, companies offer a performance bonus based on the achievement of corporate, divisional and (individual) goals. In this instance, it's a question of the percentage of the weightings – the **closer** an employee is to the bricks and mortar – the **higher** the personal weighting should be relative to corporate performance.

A number of companies use the bonus to top the employee up to the mean range of the industry compensation scale – let's call this for what it is – **a salary deferral**. Short and long-term incentive programs should provide the employee with “**direct line of sight**” or clarity in understanding what specific actions they must take to ensure that expectations are met or exceeded in order for the company to achieve superior value.

In an industry where the quality of relationships and transactions often underwrites a successful real estate asset, one must be careful that the compensation architecture and review programs have not been designed to simply satisfy legislated equity compliance, or ease the management burden of employee appraisal and job evaluation.

Alas, for many of you – these comments on compensation architecture are moot, as it would seem to me that Compensation design doesn't seem to be an overriding concern for most companies. The preference for being market competitive in salaries – seems to trump performance based architecture. However, I believe you can have both.

Compensation and Corporate Governance

The linkage of compensation to short and long term performance measures has never been more vital. It's becoming a question of governance. **There is a potential for abuse when bonuses are heavily weighted to short-term financial results.**

With "corporate governance" having become a top-of-mind issue, management may want to ensure that their compensation architecture, and that of their employees provides the Board of Directors and/or Trustees with some degree of assurance that benefits, base compensation, perquisites, bonuses and long term incentives are aligned with corporate goals and market realities. A compensation program should be designed in a manner, which induces behavior that the corporation needs to move forward to achieve superior shareholder or unit holder value.

Compensation design has not caught up with the realities of an industry where non-corporate officers are able to commit their firms to significant liability, or influence asset values with tactical rather than strategically grounded decisions. **A majority of the current structures are overly dependant on short-term financial performance measurements**, and do not adequately contribute to long term organizational effectiveness.

Rewards based solely on short-term performance foster tactical decisions. When the tactician supplants the strategist in decision-making, questions related to "governance" by stakeholders are sure to follow.

Achieving superior returns over time relative to an industry index of performance is the ultimate goal for company stakeholders. Designing a compensation plan that drives superior performance at all levels of the company is a powerful message to stakeholders and/or clients about the firm's aspirations.

Knowledge Gap Impact on Succession and Organizational Design

In summary, the Canadian commercial real estate industry failed to attract a generation of professionals in the nineties, and has been remiss at actively developing our existing middle tier talent. Clearly, we have an aging workforce.

Over the near term, I'm not convinced that the industry has sufficient time to groom, or locate enough knowledgeable top tier P&L oriented executives to support the

Strategic Business Unit (SBU) organizational structure, which has become prevalent within the industry.

In isolation, a firm would be able to source the necessary strategic talent, however all firms in five plus years will be looking for the same “innate” leadership skill sets. Demographics may well dictate a return to a centralized organizational structure; or at the very least, a hybrid structure where internal infrastructure services are centralized.

Summary

If one subscribes to current management theory, then you will agree that the essential assets and strengths of a property reside in the people that nurture its life cycle, and therefore corporate investment in education and skills development becomes a priority. **To retain your most valued people, they need to know you value them** - more often than not – mentoring, coaching and recognizing them carries greater rewards than money.

The baby-boom bust and the ensuing knowledge gap may well push some companies to the brink of organizational chaos, however the industry itself with all of its complexity has proven its resilience in the past. It truly is a complex adaptive system, which can neither be directed nor controlled – if you’re an entrepreneur with a proven track record in creating wealth – if you’re an employee that is adaptive – creative and resilient - money and/or opportunity will coalesce around you.