



The second of a series of reports from ASB on the impacts of the global pandemic on real estate investing and markets.

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COVID-19 Impacts Office Demand

COVID-19 and Future Office Demand: The Impact of Remote Work

Entering its sixth month, the COVID-19 pandemic has led most office tenants to encourage remote work and reduce employee density in office space, seeking to keep workers safe as long as the virus remains unchecked. For now, in-place lease obligations require most tenants to maintain their office footprints and meet rent obligations. Although conceptually de-densification could increase overall demand for space as employees return to their offices, greater adoption of remote working could more than offset lower density office environments. It could also lead tenants to decrease office footprints and realize cost savings when choosing future office space at lease expiration. In the wake of COVID-19, ASB examines the most impactful factors potentially driving long-term office supply-demand fundamentals.

Work from Home Appears More Entrenched

COVID-19 has changed many employers' perceptions of work from home. Significant advances in telecommunications and collaboration software now allow companies to maintain critical operations with a remote workforce. This flexibility eliminates costly and often lengthy employee commutes, affording workers greater efficiency in managing some domestic tasks and often creating better working conditions, particularly for non-collaborative jobs. In a recent survey, 44% of workers say they would prefer to work from home at least part time post-COVID, and data suggests that employers plan to offer the benefit more frequently¹. The findings suggest that as employers compete for highly-skilled workers in a knowledge economy, they will try to accommodate employee work-from-home ("WFH") preferences or risk a competitive disadvantage.

The Office: An Enduring Institution

Although employers appear more supportive and employees show greater interest in remote work alternatives, traditional on-site office use should remain at the center of organization work practice. Work from home is not new and has been used by companies for more than 20 years as technologies have advanced. Just prior to the pandemic, leading companies including IBM, Yahoo, and Aetna, had reduced work from home options, highlighting the importance placed on the office in driving employee performance. Since the pandemic, some companies like Facebook with flexible work-from-home policies have actually committed to expanding office footprints, highlighting the expected durability of office demand. In fact, Cushman & Wakefield tenant surveys indicate 90% of office workers want to return to the office, while 78% of employees also want expanded WFH options. And a separate survey of 2,300 U.S.-based workers found 70% preferred to work in the office the majority of the time, three days a week or more¹. For many people, working

away from home can help achieve better work-life balance. In particular, employees with small children find the office may be the only available space conducive for a productive work-day. In addition, managers and leaders have been challenged to foster company culture and core values remotely as well as mentor and support their teams. Operating in office space not only can improve knowledge transfer, training, onboarding, and mentorship, but also nurture creativity and collaboration—all critical to bottom line results.

COVID's Impact on Urban Cores

How would increased remote work affect urban centers if some residents seek cost-of-living and quality-of-life advantages in less-dense suburbs or even exurbs? Although a dramatic shift is unlikely, the outmigration risk could intensify the longer urban residents cannot benefit from the 24-hour attributes they have paid a premium for in pedestrian-friendly big city environs: quick commutes, mass transit alternatives to the car, vibrant cultural and entertainment amenities, the restaurant and bar scene, and expansive parks. Arguably, once the pandemic abates these important urban attractions will re-emerge as demand drivers for urban core office and residential space. Going forward, downtown "headquarter" markets are expected to continue to house key leadership and knowledge workers integral to organizational decision-making, innovation and growth. Based on our analysis, we find work from home utilization is highest in satellite office markets and lower in urban headquarter markets where collaboration among decision-makers tends to increase the need for in-person meetings. An analysis of all markets with populations greater than one million reveals that satellite markets—Raleigh, Portland, Denver, Sacramento, and Charlotte—score the top work-from-home utilization rates. Conversely, headquarter markets like New York and Silicon Valley rank lowest in work from home utilization². But large urban markets could be vulnerable, if financial distress exacerbated by the pandemic erodes essential services and leads to higher tax rates, undermining their competitive edge.

The Risk to Co-Working Space

Perhaps the office market segment most at risk post COVID is co-working space. Over the past decade co-working has expanded dramatically in some markets, becoming a critical demand driver for improved office fundamentals. Landlords had promoted the benefits for freelancers and small companies to work in collaborative environments with various office amenities like meeting rooms and administrative services. Arguably, this innovation in the office format brought many workers out of their homes and back to the office environment. The pandemic has precipitated a meaningful pullback in demand for this month-to-month space as tenants revert to the rent-free work from home alternative. Any longer-term contraction in co-working catalyzed by the pandemic could further disrupt certain office markets (particularly New York City), which had become dependent on growth in this space.

The New Office: A Post-COVID Perspective

Ongoing worker safety concerns related to the pandemic should lead to more permanent building-specific improvements as landlords seek future advantages to compete for tenants. Important COVID-19 building owner and manager initiatives include: re-engineering lobby ingress and egress protocols to facilitate social distancing, employing touchless temperature checks, installing touchless fixtures, enhancing air filtration systems, improving the aesthetics of stairwells to increase their use, and incorporating UV lighting to neutralize both viral and bacterial pathogens. These initiatives should attract tenants seeking a safe environment for an office centric workforce.

Companies that increase work-from-home options will need to decide whether to utilize desk "hoteling" where employees do not have assigned work spaces. Hoteling does allow companies to reduce their footprint and space costs, but employees prefer having their own space. Post COVID infection concerns may also influence this decision.

Summary

As a forced mass experiment, working from home has exceeded expectations and will give employers increased flexibility, which may lead to decreased office demand or simply be used as another recruiting tool to persuade top talent to join organizations. Companies will be reluctant to make radical shifts especially during the ongoing pandemic. In particular, organizations will be concerned about giving up the benefits of working collaboratively in an office environment, which can be a critical performance driver and essential for developing corporate culture. Since office lease terms generally range from five to 15 years, the impact may take time to play out.

¹ Gensler; 'U.S. Work from Home Survey,' May 2020.

² Census; Dingel, Jonathan and Neiman, Brent, 'How Many Jobs Can Be Done at Home?,' April 2020



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