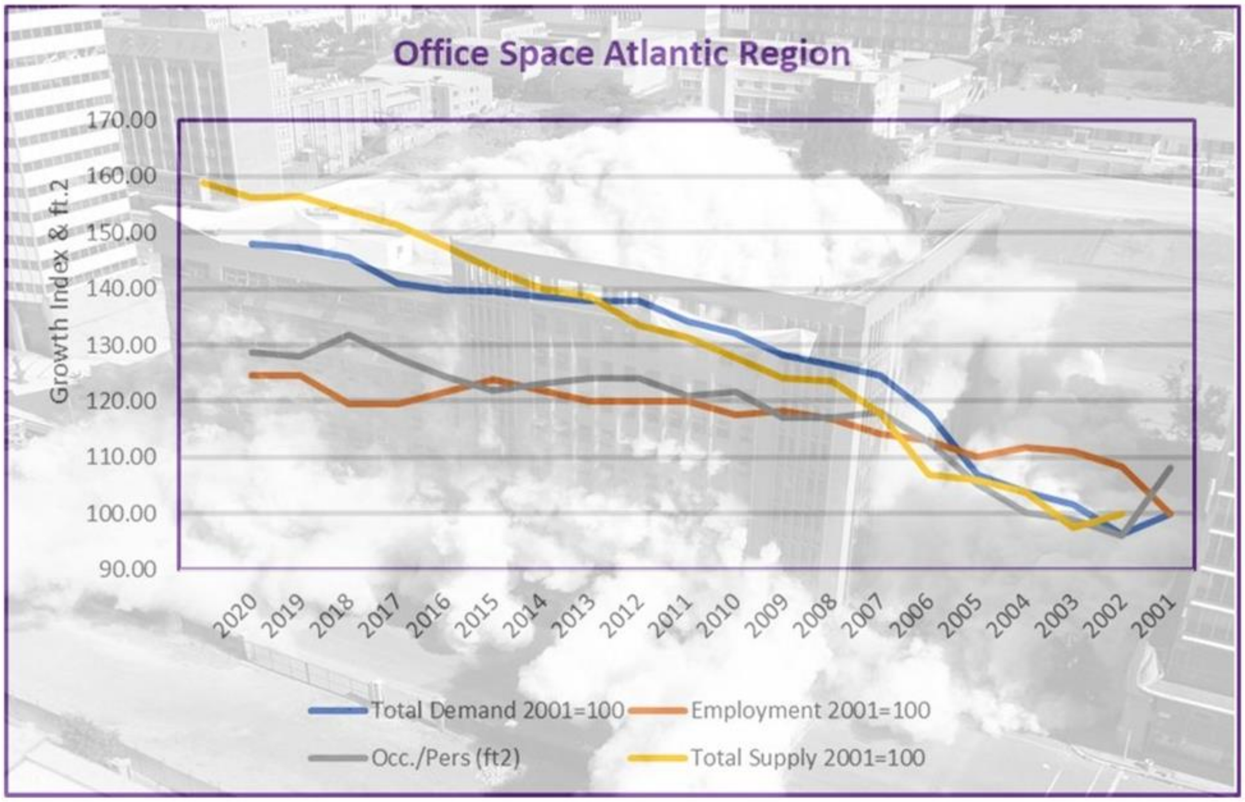
The Future of Office Buildings in a Post Covid World



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The present Covid crisis, and the necessity to embrace social distancing, has rendered working in a traditional office environment, located in a Central Business District, impractical in many cases. Savills, an international real estate broker, calculate the New York subway system "rush hour" would have to be extended to fourteen hours to safely accommodate commuters journeying to work in Manhattan. About ten hours each day would be spent commuting… in addition to another four hours entering and exiting the high-rise office building. Time for two hours' sleep then before starting on the next eight-hour work day! The impact of social distancing on commute times is less dire in Atlantic Canada but the building entry-exit constraints remain. At present most workers shun high rise office environments and continue to work from home, a situation that may only be resolved by an effective vaccine. Given that Health Canada has now started to distribute vaccines, and have pre-ordered quantities from seven firms, (three of which, Pfizer, Moderna and AstraZeneca, having efficacy rates of 70% to 95%), half the population should be vaccinated by September 2021 according to the Federal Government. Things may return to "normal" then by 2022. But what will that new "normal" look like for the office sector?

Until the coronavirus breezed into this Region in March 2020 the trend for the past decade here and worldwide favoured "collaborative work environments". Walls were removed to encourage interaction, benches replaced cubicles, informal meeting spaces, refreshment stations and lounges encouraged the mighty to rub shoulders with the unwashed, pool and ping pong tables released a flood of creative juices. The media reported that managers and workers alike welcomed the new paradigm enthusing that productivity had soared as enhanced social interaction sparked new ideas and co-operation. This was the future! Then Covid-19 reared its ugly head and everything changed; social distancing replaced interaction, working remotely from home rather than the office became the order of the day, Zoom meetings substituted for personal contact. This new paradigm too has been greeted with enthusiasm by managers and workers according to the media: non-productive commuting time has been replaced by longer working hours, routine and conformity by a more relaxed workstyle conducive to creative thinking and enhanced productivity. The enterprise's overheads can be reduced too. Even if the firm cannot operate entirely "virtually" its physical presence can be reduced, "hot desking" can be provided to service the occasional office visit. A more modest storefront can reassure less sophisticated clients or customers that the firm is not the figment of a call centre in some distant land. The disruption caused by Covid-19 has been greeted by many experts as an opportunity to re-envision the workplace, to reposition it in a virtual rather than a physical environment. The Royal Institution of Chartered Surveyors (RICS), the globally recognized body of property professionals, recently hosted a webinar on "reimagining the office and purpose of place". Workplace and property experts from both sides of the Atlantic, some of whom had worked virtually prior to the pandemic, recognized the opportunity to permanently restructure the work environment but offered a more nuanced view of the downtown office as a communications hub and a part time workspace for staff, to supplement home or suburban office workplaces. Firms recognise the opportunity afforded by Covid-19 and are struggling to determine the optimum workspace configuration once the pandemic has been vanquished. As The Economist magazine pointed out in its September 12th – 18th issue it is a matter on which there is no consensus; *"on August 28th Pinterest, a social media firm, paid $90m to end a new lease obligation on office space near its headquarters in San Francisco to create a 'more distributed workforce'"* while the same month "*Facebook signed a new lease on a big office in Manhattan"* and "*Bloomberg is reportedly offering a stipend of up to £55 a day to get its workers back to its building in London"*. In a different article in the same issue they reported that *"Jack Dorsey, the head of Twitter, says the company's staff can work from home 'forever' but Reed Hastings, the founder of Netflix, says home-working is a 'pure negative'.* There is the added complication that many cities globally are taking advantage of the pandemic to permanently reconfigure their Central Business Districts by converting traffic lanes used for vehicular parking, deliveries and circulation, to dedicated bike lanes. Halifax, Nova Scotia is a prime example of this type of re-configuration. The objective is to increase the health of citizens by encouraging exercise and to combat climate change by discouraging private cars. Amsterdam in Holland is the biking benchmark… albeit it has trams, canals, little snow and no hills. Reconfigured CBDs will be more pedestrian friendly but much less accessible by vehicular traffic.

The Future of Office in a Post Covid World

Significant emotional events such as conflict, floods, fires, recessions and pandemics change the course of history… and Covid-19 has changed working habits across the globe. Home has replaced office as the traditional work environment reversing a trend which started in the 18th century. Will this situation endure after we have an efficacious vaccine (hopefully) next year? From an employee perspective the benefits are no commuting time, a more relaxed atmosphere, on-site home care for the children and dog, remote access to office resources, and flexible hours. Satisfaction for working from home appears to be high, albeit strongly dependent on "*having a strong positive connection to their supervisor while working from home"* according to Forbes magazine. The commonly cited downsides of working from home are longer hours, more virtual meetings, lack of access to equipment, blurred lines between work and family life (the latter manifesting itself in the inability to put work aside when the day is done). Loneliness, the inability to bounce ideas off colleagues, concern about being overlooked for promotion are also issues. Satisfaction with home working is higher if there is a dedicated work space and few distractions such as young children. From an employer's perspective this workplace model offers the opportunity to reduce office rent and on-site servicing costs. It is a question whether this is outweighed by the additional costs of servicing personnel working from home, and the benefit of having everybody in the office. Although employees working from home can be more productive if the firm is geared up to work remotely and the employee has a dedicated workspace, adequate broadband, IT resources and the opportunity to work uninterrupted by family demands, there are downsides. The firm will incur costs supporting the outside personnel, particularly IT support and redirecting telephone enquiries. There is also the difficulty of coordinating tasks, training, quality control, accessibility, supervision, and lack of interaction. These may not be so much of an issue when the assignments are mundane and can be programmed e.g. work typically undertaken by call centres… or where the employee typically operates individually as is the case with many sales positions and senior personnel. However, work that is of a creative or collaborative nature benefits from personal interaction. While there are good collaborative tools such as Microsoft Teams and opportunities to meet "face to face" on line, they and the stilted world of Zoom conference calls do not yet replicate personal contact; ideas are frequently the result of chance meetings, impromptu remarks and the accidental clash of opinion. The firm may have concerns too that employees working from home become isolated causing morale and team spirit to erode. The decision whether a firm should adopt a 100%, partial or 0% remote working model post pandemic will depend on the character of the company and the functions its employees perform.

The Data Points

There was a trend to remote working prior to the Covid-19 lock downs. The movement started at the beginning of the 1990s and was initiated by a major recession which called into question the economic justification for prestige office space in Central Business Districts. It was facilitated by the emergence of the internet, mobile phones, software and hardware designed for remote working. Firms started to move their offices out of downtown areas into industrial parks or abandoned them completely and required their personnel to work from home. As technology improved the trend gathered impetus. Although Covid-19 has had a more dramatic impact on work habits than the 1990 recession its effect is more of timing than scale… it will exacerbate the existing trend, expediting change that would have occurred anyway. Examination of the workplace trend since 1990 therefore allows us to determine the future face of the office market in the Atlantic Region, and to a large degree the fate of its Central Business Districts, and to determine whether the office market will wither in the face of remote working. The 1990s decade was dominated by the recession and a market meltdown. Things improved gradually but it was not until the dawn of the twenty-first century that the Region's office markets put the events of the prior decade behind them and normality returned. The period post 2001 provides us with an insight into the fate of the office market once Covid-19 has been banished, hopefully by the end of 2021. By happy co-incidence we have tracked office supply and demand in all five of the largest metropolitan areas (St. John's, Halifax Regional Municipality, Charlottetown, Moncton, Saint John, Fredericton) since 2001. By that date office supply and demand was approaching equilibrium and the overall vacancy rate was a manageable 8.30% (equilibrium vacancy is generally considered to be 5%). Office developers started to build again, as did office demand.

Our graph on Page 1 captures the aggregate office market in the Atlantic Region during its post-recession phase from 2001 to the present day. For comparison purposes we have indexed total supply, demand and employment to the common base date of 2001. It appears counter intuitive given the trend to home working, but demand grew steadily from 2002 onwards before it plateaued in 2013-2016, and then grew again in 2017 (the St. John's and Saint John office markets were adversely impacted by the steep fall in oil prices mid-2014; crude oil prices bottoming out in 2016 and then gradually starting to recover). The Region's developers responded by starting to expand supply in 2001, were caught short by the oil crisis and overshot the growth in demand in 2013, and continued to bring product on-stream during the pause in demand. The growth in office demand is even more surprising given that growth in employment has not been robust. The Atlantic Region's population is aging faster than the rest of the country but the provinces were slow to recognise the problem until the publication of the Nova Scotia Commission on Building our New Economy (Ivany Report) in 2014. They have since been successful in attracting more immigrants from overseas, returnees from Alberta's oil patch, and retirees from elsewhere in Canada, to help boost the economy and employment. However, it is a slow process and most of the increase in office demand appears to be due to the amount of space occupied by each employed person. As our graph illustrates it increased from 108 ft2 in 2001 to 129 ft2 in 2020. Given that the trend during this period was to reduce the amount of space per head of office staff in order to promote social interaction, the data infers that office staff who started to work remotely in the aftermath of the 1990 recession returned to an office environment post 2000 in sufficient numbers to counteract it. This suggests that the Covid-19 inspired "work from home" phenomena will be a blip rather than a trend. While remote working will continue after the distribution of an effective vaccine, office personnel will gradually return to office buildings. The work model will continue to evolve to a more mobile workforce but the benefits of social interaction on productivity will outweigh the rental gains achieved by ditching the office completely. We forecast therefore that most private sector employees will return to working in an office environment when a sufficient proportion of the population has been vaccinated to alleviate Covid-19 concerns (probably towards the end of 2021: public sector workers will take a little longer). Depending on the type and culture of the employer, remote working will be more prevalent than was the case pre-Covid but this will be balanced by a gradual drift back to an office environment over the next two decades. Some staff will continue to work remotely for part or the entire work week. Central Business Districts will be slower to recover than the suburbs in large part because office working has already restarted in the latter. Many suburban buildings, particularly in the industrial parks, are low-rise structures where safety and access issues are less of a concern. We anticipate that the stigma attached to high rise buildings will dissipate fairly quickly. The demolition of the World Trade Center's twin towers by Al-Qaeda terrorists on September 11th 2001 must have created a sense of unease to occupants of high-rise buildings but there is no evidence that it reduced space demand in this region for any significant time period.