

The office of the future - and implications for Office REITs

By: Brendan McCarthy | August 25, 2020

Washington - Are you reading this article from your office, surrounded by your keyboard, mouse, pen, papers and ... a child or dog running around the house?

With the rapid rise of COVID-19 earlier this year, almost every office sent their employees home in an effort to keep them healthy and arrest the spread of the virus. This was an unprecedented, natural experiment in remote working. While not without glitches, the result has surprised those corporate leaders who expected a massive drop in productivity that never materialized.

The advantages of working from home (WFH) are a lack of commute and a flexible environment that attracts, enables and retains talented staff. The disadvantages are potential feelings of isolation, communication hurdles (both technical and social), training difficulties, challenges in building and maintaining a team culture and at-home distractions. Therefore, a hybrid model is likely to emerge, with employees splitting time between home and office.

Dueling demands for office design

On its own, an increase in people working from home would likely cause a decrease in overall demand for office space. However, countering this is social distancing policies that will require more space per employee as offices reopen, reversing a long-term trend of increasing office density. Over the past 30 years, office density has shrunk from 300 SF/employee down to as small as 75 SF/employee for some coworking spaces, according to Union Investment Real Estate GmbH's Tal Peri.¹ That trend is expected to reverse as employees start returning to work, and major office landlords are already considering how this will impact their spaces.

We think the decrease in demand for office space from WFH adoption likely will be offset by an increase in demand for space per employee, with the net effect being a small net change in demand in either direction. But we also expect significant disruption in office building design, disruption that we believe will generate outperformance from office REITs that focus on the social elements of their buildings.

Increased focus on healthy design

Going forward, office tenants may increasingly seek office space that is suited for collaboration and tenant health and safety, key tenets of the growing healthy building design trend. Healthy design takes into account scientific research on environmental health, behavioral outcomes, health outcomes and demographic risk factors that affect health and wellness. Through the use of improved air ventilation, natural light and materials, quality acoustics, indoor-outdoor space integration and other elements connecting architecture to nature, healthy buildings can promote the wellness and productivity of their occupants.

Healthy building design was a small, but growing, niche prior to COVID-19.² The onset of the COVID-19 health crisis is accelerating this transition, with the most immediate attention on improving air quality. According to research from the Department of Homeland Security, coronavirus particles decay faster in environments of 78°F and relative humidity of 50% - conditions associated with outdoor environments - than at lower temperatures and humidity. Incorporating UV light to mimic sunshine further hastens the virus's decay. Beyond the coronavirus, research from Yale University has shown that humans' immune systems are more resilient against viruses in warmer, humid conditions like those found in outdoor air.³

Improved air circulation will also be important as office users shift away from individual workspaces and toward open, collaborative spaces. Demand for open space will force office owners to rethink floor plan layouts. Among other considerations, they will need to explore how tenant spaces are carved up, where structural elements like pillars and walls are placed, points of egress, restrooms and how these spaces incorporate natural light and materials.

While making these adjustments will require capital outlays, a number of leading office REITs have already begun implementing healthy design, guided by certification bodies like Fitwel and the International WELL Building Institute. These REITs understand that a company's greatest asset is often its people - and keeping those people healthy and productive is a top priority.

Bottom line: As more companies make working from home a standard part of employee work schedules, REITs will need to consider the implications for office design. By offering a differentiated product that supports those goals, these offices may be able to achieve premium rents from the tenants seeking such space.

1. Tal Peri, "The Office Is Not Dead—*ust* Evolving—*ad* Definitely Here to Stay," *National Real Estate Investor*, July 7, 2020. Accessible at <https://www.nreionline.com/office/office-not-dead-just-evolving-and-definitely-here-stay?>

2. Global Wellness Institute, *Global Wellness Economy Monitor 2018*. Accessible at <https://globalwellnessinstitute.org/industry-research/2018-global-wellness-economy-monitor/>. Elizabeth Wallace, "Why the Wellness Industry Means Big Business for Designers and Architects,"

3. Bob Tita, "Offices Try to Combat Coronavirus With More Fresh Air," *The Wall Street Journal*, July 8, 2020. Accessible at <https://www.wsj.com/articles/offices-try-to-combat-coronavirus-with-more-fresh-air-11594206158?mod=searchresults&page=1&pos=3>



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