MBRE RESEARCH

LOOKING PAST THE PANDEMIC:

LIKELY CRE OUTCOMES

OCTOBER 2020

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You don't have to look back at January predictions for 2020 to know that, well, things are not going to turn out as planned. And thus, we ask: what new factors are in play now that the coronavirus pandemic has altered the trajectory of the commercial real estate world? From health concerns to changing amenities and evolving lease terms, we're re-examining 2020 through the lens of what we now know.

One prediction: things are not as apocalyptic as they seem.

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#1 SUBLEASE MARKET

Companies are cutting back and looking for ways to save money. Among the easiest solutions: subleasing space. After all, if employees are effectively working from home, some companies may think twice about returning to the office at all. The inevitable increase of available sublease space will resonate throughout the office market, though the full extent remains unclear. The amount of available sublease space has been increasing daily, currently reaching 4.6 million square feet, surpassing the high of 4.2 million square feet reached during the great recession.

#2 CITIES VS. SUBURBS

The suburbs offer something to residents and businesses looking to escape pandemic concerns that cities cannot: space. Chicago's suburban housing market is seeing a significant uptick in interest from urban dwellers looking for more square footage. Businesses may follow their employees, especially since those employees will be reluctant to commute by train until the pandemic is behind us. Recently-transformed office developments in the suburbs may see more interest in the near future if companies follow their employees and decide to seek alternatives to cramped cities. However, it is more likely that companies will open smaller satellite offices in the suburbs than make the long term commitment a relocation would require.

#3 COWORKING

WeWork was imploding before the pandemic reared its head. Now, the entire industry is facing challenges that may be insurmountable. Although the short term flexible space that coworking offers is attractive in today's environment, it's also very easy to eliminate all together when tenants are looking for ways to reduce costs. The pandemic recession is the first test of the industry's ability to weather an economic storm. In addition, entire concept of "shared" space in a pandemic is problematic – a challenge the industry could not have foreseen. Coworking platforms that are able to survive the current crisis may find themselves in a strong position once the dust settles, but there will inevitably be a significant scale back of the industry that was arguably already overbuilt.

#4 SHORT TERM LEASE RENEWALS

Companies with dreams of big moves and expansions pre-coronavirus will scrap previous plans in favor of lease renewals. In fact, many tenants will likely be looking for short-term answers as they watch the world to see how the cards fall. What's more, landlords will be more amenable than ever to short-term renewals as they find themselves competing with subleases and seeing fewer tenants in the market.

#5 STREAMLINED LEASES AND SPEC SUITES

Speaking of amenable landlords, spec suites with shorter terms and streamlined leases may become more prevalent as landlords respond to pandemic-inspired predicaments. In an effort to lure small companies fleeing coworking, landlords are offering more flexibility than they have in the past. Landlords will also have to offer built out space with shorter lease terms in order to compete with sublease space. Clinging to the traditional leasing process, which is slow moving and requires substantial commitment, will cause landlords to miss out on the existing market opportunities.

#6 PUBLIC TRANSPORTATION

Streetcars didn't fare well during the Spanish flu, and the pandemic may have aided the adoption of cars post-World War I. Will modern public transportation face similar struggles? It is hard to say, but public transit definitely faces many challenges in the coming years. Lack of ridership due to fears of virus exposure will have a big effect on the economic viability of transit authorities. Economic problems due to coronavirus will impact transit significantly as ridership fares decrease and cash-strapped states attempt to balance COVID-19 overages within budgets.

#7 NEW MEASURES, NEW COSTS

New cleaning supplies, increased labor costs for more frequent cleans, testing kits and temperature-taking devices, improvements to air filtration systems, and more changes will cost a lot of money. But who will the cash for these updates come from? Will buildings take on the brunt of these costs, or will they get passed on to current and future tenants? In all likelihood, both parties will find themselves covering new fees, even as they look to reduce costs to make up for quarantine losses.

#8 CHANGING AMENITIES

Before the coronavirus pandemic, most building amenities were community oriented. Now, conference rooms, tenant lounges, and other shared spaces are unlikely to be the selling points they once were. The new amenities will be about health and wellness. Outdoor space will become a huge selling point for obvious reasons., Private gyms will be coveted. Enhanced air ventilation and filtration systems, antimicrobial surfaces, and touchless entry will be the new gold standard. In short, health and wellness will no longer be a subset of overall design—it will be a core value for tenants concerned about amenities.

IN CONCLUSION

The world of office space in just a handful of months has changed and will likely never completely go back to what it once was. With that said, these changes are not all-encompassing or earth-shattering. Subleases and infrastructure present unique problems that currently do not have answers, but that doesn't negate the fact that people still have to do their jobs; people will always have to find ways to work together. And while this pandemic will undoubtedly change some of our habits, it won't change the core fact that there is no replacement for in-person productivity.

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