



The New Paradigm: Office space occupier decision making criteria in the post-COVID-19 world



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We will emerge from the COVID-19 crisis, as we have from previous crises such as 9/11 and the Great Recession. As with each previous crisis, when we emerge, occupiers will re-evaluate their existing priorities and have new or additional priorities. Although it is too early to know the outcome of this process, we can anticipate some of the issues that will be considered to allow executives to make the most informed decisions for their organizations. This paper addresses some of the major decision-making criteria that will likely be in play and presents a series of questions and prompts that stakeholders may address in the post-COVID-19 environment.

Real Estate Strategy

In order to develop a real estate strategy for an organization, real estate professionals should apply a programmatic approach, including an evaluation of the organization's demand side needs considering finance/accounting, labor, workplace design, wellness, technology and risk mitigation, and overlay supply side conditions globally or nationwide and in each local real estate market. Some business considerations will be critical to address:

- a. **Strategic Planning:** The first step should be to understand how the organization has historically conducted its business and how peer organizations have conducted business, and to consider how that should change in order to reflect a changed post-COVID-19 world.
- b. **Portfolio Planning:** The re-assessment of labor, technology and workplace design will result in or reveal a misalignment of real estate assets/leases for many organizations. These organizations will then need to evaluate the costs and benefits of migrating to an optimized real estate position. A transition plan may need to be developed as wholesale change will be difficult to produce in the short term, particularly in dislocated markets and with company balance sheets stressed due to the business slowdown.
- c. **Re-balancing Annual Cost, Total Cost and Flexibility:** For many organizations, annual cost has been the over-riding decision making criteria. Taking a back seat to annual cost has been the overall financial obligation, capital investment (at times), and flexibility (and the cost to implement). As we emerge from this crisis, organizations may perform a forensic audit on how the structure of their real estate position or how their specific contractual obligations enabled or inhibited their organization's ability to respond and perform.
- d. **Quality:** Quality will become pervasive in all aspects of the real estate decision making criteria. Credit quality will play an even more important role than pre-COVID-19, as high credit quality organizations will be best positioned to use their financial wherewithal in traditional manners such as financial structuring and access to capital, and will

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also leverage their demands for changes in areas such as force majeure, casualty, and other formerly legal, now economic, terms that will be negotiated earlier in the process. On the building side, there will be a continued flight to quality as newer properties offer more advanced HVAC systems and other building attributes that support a healthier work environment. Lower quality buildings will need to consider significant capital investment to compete.

Labor Strategy

The long-term impacts of COVID-19 on workforce location strategy will be determined over many years, but already a few critical questions have been raised that challenge the current state. Co-location of knowledge workers in order to foster innovation is considered best practice behavior and has delivered proven results. That said, awareness of the risk of spreading infectious diseases will persist and more scrutiny will likely be applied to identifying which functions/workers actually contribute to the chain of innovation and to what degree. This risk could lead to a number of potential outcomes:

- a. **Geographic Diversification:** Companies will place more emphasis on strategically locating employees with specific skill sets to de-risk critical functions from complete loss of productivity in the face of future pandemics.
- b. **Hub and Spoke:** Within a single market, organizations may opt for more hub-and-spoke labor catchment models (one large HQ site with multiple pods around market) with the goal of diversifying where employees reside and their commute methods.

Ultimately, companies will need to navigate the core tension between bringing knowledge workers together in a consolidated environment (single city or site) and the risk of future pandemics in major cities.

Workplace Strategy

In the economic growth cycle that has abruptly ended with the COVID-19 pandemic, the workplace has been transformed significantly. Companies have shifted the emphasis of their real estate decisions to provide greater focus on the workforce. This transformation has benefited Human Capital by providing work environments that recognize the differing desires of the various demographic groups within the office, while continuing to provide economic benefits to Finance and Accounting through space compression, resulting in lower overall occupancy cost. Many of these workplace decisions will now undergo examination, as social distancing and a greater emphasis on a sanitized work environment become part of the decision criteria.

- a. **Hygiene:** Germs will be a focus as we go back to work, with social distancing and other sanitization protocols in place.
- b. **Wellness:** The health factors of buildings are going to have greater importance than we saw previously, putting more emphasis on everything from cleaning services to ventilation and operable windows. What about the possibility of shaping building amenities with a greater slant to address on-site medical needs and preventative measures restricting “sick” workers or guests from entering the building or work space?
- c. **Mobility:** The Genie is out of the bottle. Teleworking will be the other long-lasting take away, with the benefits to employees and employers obvious from this “required experiment”. Countering the movement towards work at home is the challenge presented of managing a remote workforce, bandwidth limitations in some geographies, and the productivity of long-term remote working, as working from home may become less productive the longer a worker works from home.
- d. **Densification:** Many organizations have increased densities up to 50% over the past two cycles. The current levels of density and openness will be juxtaposed with the desire for physical distancing, teleworking, cleaning, and health and wellness.
- e. **Culture:** As much as workplace focused on “culture” before this moment in time, companies are getting a crash course in learning how culture can be relayed virtually through policies and digital experience of employers and colleagues.

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- f. **Holistic Approach:** In the end, employees will bring back the strengths of more versatile physical and digital work practices. The buildings that best serve the wellness and performance of their occupants will continue to play a stronger role in real estate decision making. This will likely accelerate the flight to quality that we have seen during the previous real estate cycles.

Technology Strategy

The broadest theme is that COVID-19 is forcing organizations across the span of the technology literacy spectrum to adopt tools and ways of working that have been prevalent across industries for the last decade but perhaps not fully adopted before now as the new “standard”. In light of the unprecedented changes being forced through the system—“holding out” and not learning these new ways of working is no longer a feasible option for even the most recalcitrant end users. This will fundamentally shift the “standards” across businesses as we move into the post COVID-19 world. The better tools will shine as more users engage and ultimately push their respective companies to adopt user-friendly interfaces for their workforces, displacing the legacy systems that are still entrenched in some companies.

- a. **Meetings:** In-person meetings become a luxury option versus remote video meetings which become acceptable en masse and standard.
- COVID-19 forces “holdouts” within the broader workforce to i) learn the tools, ii) spend time thinking about what makes a good remote meeting, iii) understand that communicating virtually is different (should be done differently) than in person, and iv) become reasonably competent at hosting/participating in remote meetings and communications.
 - Face-to-face meetings are still more desirable but given the travel cost (and potential near-term aversion to travel) will likely be viewed as a premium/luxury option for some period of time (or longer).
 - Town-hall style meetings have often required large dedicated spaces and/or the renting of event space—Zoom and similar video meeting technologies have proven quite effective for these purposes and we will likely see a long-term adoption for these needs.
- b. **Applications:** Mobile apps (with seamless cross-platform interfaces) and cloud-based infrastructure become standard for modern organizations.
- It’s difficult to imagine this is ground-breaking, but it’s also difficult to imagine companies not using cloud-based systems such as box.com or dropbox.com for file storage; mobile on-demand apps that connect through the cloud and seamlessly update across devices continue to please users with simple interfaces and easy remote access—they have gained widespread acceptance in the COVID world and will be the standard moving forward.
 - On-line document collaboration (most widely used by students on Google Docs) has greatly accelerated in the corporate world now with similar products including Office 365.
- c. **Documents:** Digital signatures and contracts gain necessary traction to become acceptable standards across industries.
- This also is not ground-breaking, but the remote environment is yet another example of how tools like DocuSign may become the standard for contract management going forward.
- d. **Learning:** Remote learning gains traction and investment.
- Similar to meetings, it’s one thing to use a tool to host remote meetings, but we will likely be entering a world in which the tool must be good at hosting remote learning meetings. Teaching tools will need to go through a reality check on how to effectively teach remotely—what it takes, what sticks, what works, etc. What is interesting is that it’s happening under a microscope in every family with children at home right now trying to learn. These at-home experiences will make their way into the workplace. There will be winners and losers, and the winners will garner investments in tools, frameworks, and workforces that are effective at remote teaching and learning.

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Risk Mitigation Strategy

As the COVID-19 crisis has revealed with surprising clarity, the generally accepted norms for building operations, legal protections, and insurance have exposed occupiers to unacceptable risks. Occupiers will need to develop strategies to mitigate these risks moving forward, as we all now understand that pandemic-related risks are more serious than the risks usually focused on such as fire, flood, or equipment breakdown. Specific areas that will require a new approach include:

a. Lease Clauses, for example:

- i. **Force Majeure:** Force majeure clauses have not typically benefited the tenant as an exclusion to force majeure remedies is the obligation to pay rent.
- ii. **Service Interruption:** Service interruption clauses have not typically been structured to provide relief against pandemics because often those clauses have not included “access” as a service and have excluded interruptions beyond the landlord’s control.
- iii. **Casualty:** A typical casualty clause has provided rent abatement only if the premises, or sometimes the building, is physically damaged.

b. Insurance: When buying insurance, occupiers need to understand and push back against the limitations of business interruption insurance.

c. Building Operations: As previously addressed in the Workplace section, greater scrutiny needs to be given to base building systems, building performance, and the building operations specifically relating to health and wellness, cleaning, access, security screening, and rules and regulations to protect both the occupier and the owner. Companies may want to gain control over some of the services currently performed by landlords, particularly cleaning.

d. Operating Expenses: With the expected improvements to building operations comes increased costs to operate. Occupiers will make greater demands that owners bear some of this increase, rather than passing all of the cost increase onto the occupier through the operating expense pass-through. For 2020, occupiers will need to carefully review the reconciliation statements, as landlords will incur increases in certain costs, with likely offsets to others due to mostly vacant buildings during the crisis period.

Key Take-Aways

COVID-19 has created disruption on a massive scale. As we emerge from the storm, there will likely be a strong desire to normalize life, so a swift movement to significant change may be viewed as continuing the disruption rather than a slower, more incremental approach to change. As is human nature, most things will revert to the past practices, with changes occurring in those areas that can be proven to enhance an organization’s ability to deliver its mission through good times and bad.

Note: Part two of this series, which will include tools to use to address the above-mentioned topics, will be published in the coming weeks.

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