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**Workplace  
Roundtable  
2021**

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# Pandemic challenges working assumptions

*Participants at PERE's workplace roundtable discuss the radical changes underway in the once-predictable office sector. **Stuart Watson** reports*

This is the first time in my career when we are asking the fundamental question of what an office is for, and how people will use it," muses Nuveen Real Estate's Nick Deacon. That such a statement could come from the head of European offices at one of the largest global managers demonstrates the extent to which investors are reconsidering the post-pandemic role of an asset class that is the mainstay of many large private real estate portfolios.

That existential inquiry is the jumping-off point for *PERE's* inaugural workplace roundtable discussion. While the effect of the pandemic, for better or worse, has been easily discernible in other property sectors, the jury is still out on what the lasting impact on offices will be. Last year, many investors hesitated to commit capital to the segment in the quantity seen before the pandemic. RCA data show that in the Americas the asset class's share of

deal volume fell to 23 percent in 2020 from 26.5 percent in 2019, dipping below that of industrial for the first time. Meanwhile in Europe, the proportion fell to 39 percent, down from 44 percent in 2019, marking the first occasion on which it has slipped behind the combined total for apartments and industrial.

RCA's analysis of net acquisitions by the top 100 global investors in 2020, which totaled \$65.4 billion that year, down from \$83.7 billion in 2019, further demonstrates the increased caution among major capital providers. Those firms added just \$11.3 billion more office assets to their portfolios than they sold in 2020, a 49 percent pace of decline from 2019, whereas the industrial sector saw only an 11 percent fall in the pace of net investment.

### Cultural shift

Working from home has been the norm for many white-collar workers during the pandemic, and investors are questioning whether it will create a

precedent that has a serious impact on the post-covid demand for office space. A clear cultural shift has occurred, argues Jeb Belford, managing director at New York-based manager Clarion Partners. "Whether it is permanent or not remains to be seen. But for now, gone are the times when you had better have a good excuse why you are not in the office, particularly in some segments of the market."

Deacon observes that many occupiers are still grappling with the immediate impact of covid-19 on their bottom line, and therefore have not yet taken a long-term view on the future of their corporate estates.

However, he too believes that attitudes have evolved. "The balance of power is with the employee not the employer. There will be a continued threat around covid, so the voluntary approach towards running the gauntlet of public transport to come into the office is going to be prevalent.

"Our own business has just gone through an exercise to look at the

## Frank RoccoGrande

Founding partner  
Deutsche Finance International

RoccoGrande is co-managing partner of London-based global investment manager DFI, which he co-founded in 2016. The firm specializes in operational real estate and pursues core-plus and value-add strategies. It is part of Deutsche Finance Group, a global real estate investment management company with more than \$9.1 billion of assets under management, around a fifth of which is in the office or life sciences sectors.



## Jeb Belford

Managing director  
Clarion Partners

Belford joined Clarion over 25 years ago. He is an equity owner in the New York-based manager and lead portfolio manager for its \$17 billion open-ended diversified core fund, which has an exposure to the office market of around 30 percent. Clarion has assets under management of around \$55 billion overall, around 20 percent of which is in the office sector.



## Nick Deacon

Head of offices, Europe  
Nuveen Real Estate

Deacon is responsible for leading office investment activity across Europe at Nuveen Real Estate, the real estate asset management arm of US insurance company TIAA. Nuveen manages around \$133 billion of assets globally, across the risk spectrum from development to core mandates, of which approximately \$32 billion is located in Europe, and 25-30 percent is in the office asset class.

## Bas Jochims

Director Dutch office and hotel investments  
Bouwinvest Real Estate Investors

Jochims joined Bouwinvest 15 years ago, and manages its €1.2 billion Dutch office fund. The firm invests mainly on behalf of pension funds including bpfBOUW, the Dutch construction workers pension fund for which it has the global real estate investment mandate. Bouwinvest manages around €15 billion of assets overall, about 65 percent of which is in the Netherlands.



# Analysis

appropriate level of home working, and I think that will be the case for many firms.”

Nonetheless, some employers that cast doubt on the long-term need for office space last year are beginning to row back on their earlier statements, Deacon says. “It was a knee-jerk, almost fashionable, reaction to the pandemic.” He notes recent comments by Goldman Sachs boss David Solomon rejecting remote working as a “new normal” and labeling it an “aberration,” as an example of a counter-tendency. “That is one extreme. But many businesses are not Goldman Sachs and there will have to be a change,” he qualifies.

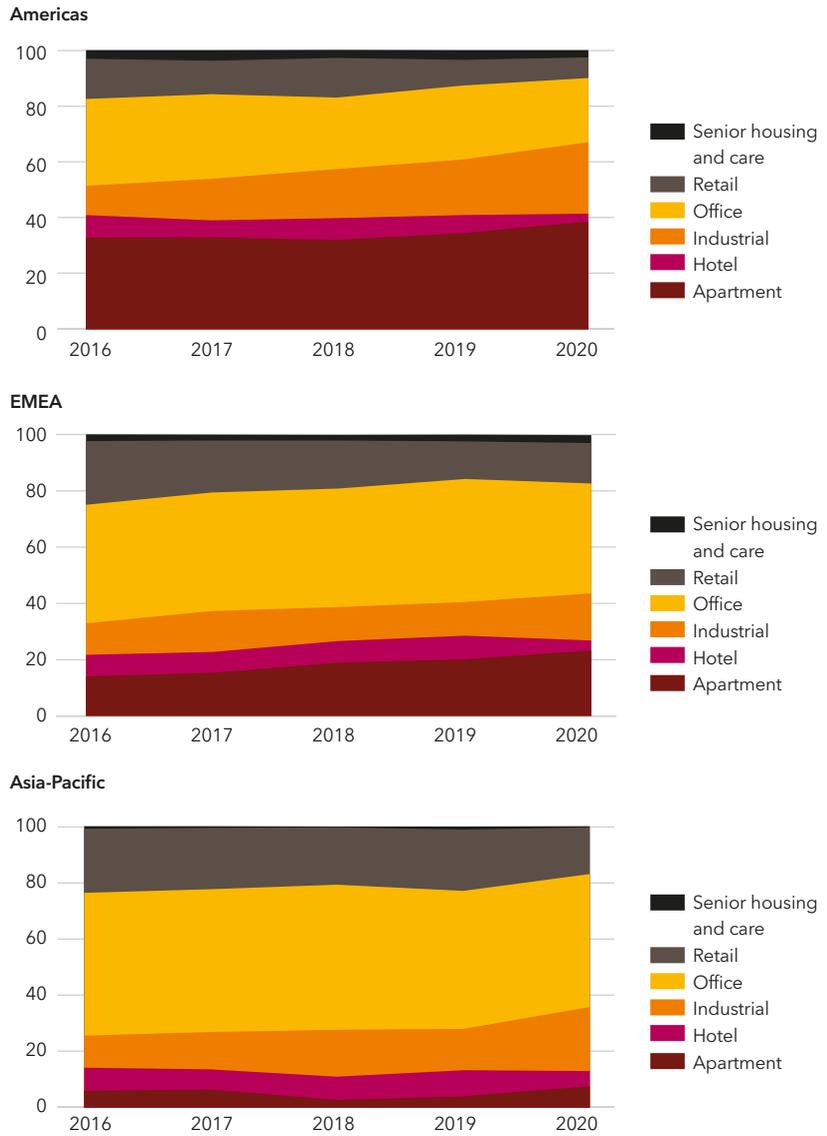
A contrast is emerging between different-sized companies, says Belford. “Large organizations are going to be more likely to reflect Goldman Sachs’ more cautious approach to home working. A lot of smaller firms may take a different approach, partly because it will help them to compete.”

## Evolution, not revolution

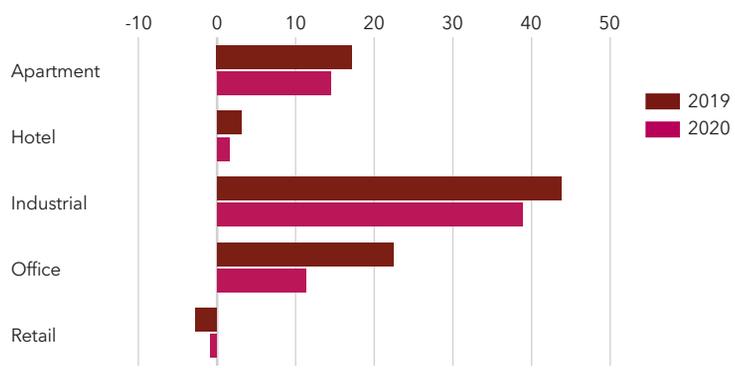
Some locations like Amsterdam, the home market of Bas Jochims, will have to do less adapting to the new paradigm than others, suggests the director of Dutch pension manager Bouwinvest’s office fund. “In the Netherlands it was already quite common to work from home. Most people worked from home one or two days a week, which is very different to some other office markets like Paris, London and New York. The culture here is already quite flexible. Most Dutch employers do not force people to come to the office. It wasn’t like that before covid, and it certainly won’t be after.”

While there will be more remote working, at least part of the reduction in demand for office space may be offset by a reversal of the trend towards densification, suggests Deacon. “That started before covid, and it will be accelerated by the pandemic. In those cities, especially London, where you have seen a phenomenal shift in efficiency of use, I suspect we will see that unwind.”

Logistics and apartments have both outstripped offices in the Americas, and gained ground in Asia, as a share of annual investment (%)



Net investment by top global investors (\$bn)



Source: Real Capital Analytics

*“Office is the sector with the biggest question mark attached to it, and it is a big sector”*

JEB BELFORD  
Clarion Partners

*“Most Dutch employers do not force people to come to the office. It wasn’t like that before covid, and it certainly won’t be after”*

BAS JOCHIMS  
Bouwinvest

Frank RoccoGrande, co-founder of private equity real estate investor Deutsche Finance International, argues that the market will see “an evolution, not a revolution,” with buildings that meet the changing needs of office users continuing to offer attractive investment opportunities, while poorer assets fall behind. “In London, for example, newly built, well-located, well-adapted buildings with a healthy environment for the end user in the West End have traded recently at pre-covid yields. That shows the flight to quality and I do not think that will change any time soon,” he says.

DFI is undertaking an urban regeneration project around London’s Olympia exhibition center, which includes 800,000 square feet of offices. RoccoGrande says that in researching the market, his firm identified eight characteristics that will characterize successful office assets in the post-covid world: accessibility, amenity, flexibility, wellbeing, the provision of collaboration spaces, smart building technology, sustainability and accreditation by benchmarks like LEED and

## Analysis

WELL. “Covid has not really changed any of those, but it has definitely accelerated them. This is a period of adjustment, and it is all about the war for talent. If office users do not adapt to the needs of the talent, they are going to lose their competitive position.”

### Impact on returns

The participants agree that while investor sentiment about the future performance of offices has been shaken by covid and its economic fallout, rent collection, returns and asset values in the segment have been mostly robust so far.

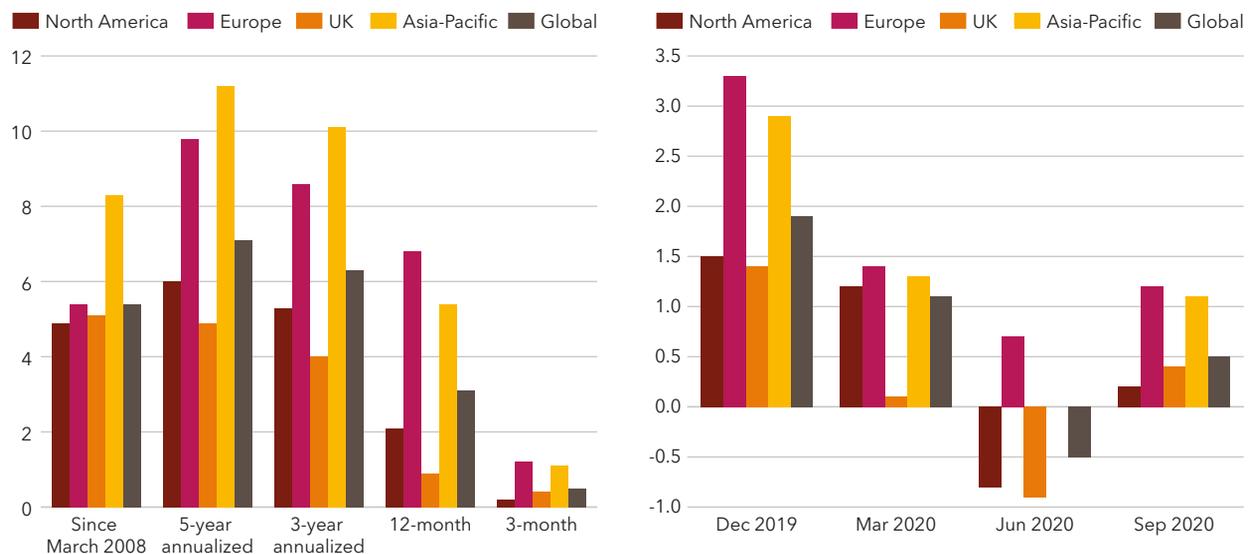
Deutsche Finance America owns stakes in several landmark US office buildings, including the CNA Center, known locally as ‘Big Red’ in Chicago, the Coca Cola building in Manhattan, and San Francisco’s Transamerica Pyramid. “We have quite a lot of exposure across prime markets in the US, and, on the whole, we were positively surprised at how resilient they were,” says RoccoGrande. “Across the board our corporate occupiers have held up well, and continue to pay pretty much on time.”

Despite instructions from Bouwinvest’s Dutch pension fund clients to be

*“We will see far more radical business plans being adopted to maintain the relevance of these buildings”*

**NICK DEACON**  
Nuveen Real estate

Office returns recovered somewhat in Q3 2020 after struggling in Q2, but recent performance remains well below three and five-year averages (%)



Data as of September 2020; returns in left hand chart are over a three-month period  
Source: MSCI

generous to struggling tenants, very few requested rent deferrals or reductions, says Jochims. “In April to May last year, we worked on scenarios for the impact on returns. But it proved too difficult to make adjustments at that time. We expected a decrease in value of 8 percent in the Dutch office market last year. However, we saw positive revaluations, and it ended up with 2 percent growth.”

Clarion found predicting the impact covid would have during the course of last year similarly challenging. “In retrospect, we were trying to make educated guesses about its effects. But none of them met with what actually played out. Actual office performance was slightly positive overall in our portfolio. We maintained our income and, on balance, we had a little bit of depreciation, which left us with a slightly positive total return for 2020,” says Belford. Value adjustments were predictably greater in cities that were worse affected by the pandemic.

The longer-term performance outlook for the asset class is no easier to gauge. “We have not had many investors expressing much angst. They are mostly long-term oriented. But at the same time, they are keen to get our view of what is happening on the ground,” he adds. “Office is the sector with the biggest question mark attached to it, and it is a big sector. While it is fairly easy to see what is happening with many other sectors, with offices it is tough.”

### Meaningful intervention

Office occupiers have received less government support than retail and hospitality businesses and are consequently less threatened by a cliff-edge decline when government stimulus packages run out, argues Deacon.

“On a relative basis, the sector looks pretty resilient. But we cannot be complacent. Anybody investing in offices in the last decade has probably made money. In the next 10 years, it will be all to play for



## San Francisco high rise is low hanging fruit for Deutsche Finance America

### Transamerica skyscraper is a long-term asset management play, says RoccoGrande

At the end of 2020, Deutsche Finance America, together with German pension fund BVK and New York-based property developer Michael Shvo, bought San Francisco’s famous 48-story Transamerica Pyramid office tower and two neighboring properties for around \$650 million. “Everyone said we were nuts going into offices at that point in the cycle,” admits DFI’s RoccoGrande. But he explains that the rationale for the transaction was based on the primacy of asset management in generating office market returns going forward. “That deal was all about location, and repositioning an iconic property that is irreplaceable. It is unlikely there will be more towers like that given the building code in San Francisco, irrespective of how much office space is on the market at any point. For a few years it has been an appallingly poor experience going into that tower, so for us it was low-hanging fruit. With assets like that you have to be willing to roll up your sleeves, and have very long-term institutional capital partners who are willing to ride out a cycle or two while you execute the business plan.”

because there will be such diversity in performance.”

There is consensus among the participants that post-covid disruptors will make offices a more complicated and expensive asset class in which to play. “Asset management will be critical in the next five years, and that will cost money,” says Belford. “Offices are always expensive investments from a capex point of view. But the future will likely see an extension of what we have been living with for a while.”

Owners will have to invest more and work harder to maintain the competitiveness of their assets, he argues. “In the US, technology firms have driven a cultural change, which has permeated across the office sector. We were already living in an environment where we had to think hard about what we want to own, and how to best position those buildings for what tenants

demand. That is even more critical today, because covid has acted as an accelerant for that trend.”

Institutions with large office portfolios are increasingly likely to turn to office specialists to apply sector-specific expertise across their holdings as the fallout from the virus wreaks its changes, says Deacon. “There is a lot of mediocre stock in capital cities. I do not think we will be able to get away with floor-by-floor refurbishment anymore. Now you have to reinvent that stock. That requires more meaningful intervention, even recladding buildings, which means getting vacant possession. We will see far more radical business plans being adopted to maintain the relevance of these buildings.”

Jochims adds that it is important not to neglect the “soft” elements of asset management. “Being very distinctive is also about stakeholder engagement,

placemaking, branding, telling the story of your asset. Is the story about architecture, or concept, or location or former use? For example, at our redevelopment of the two landmark former Citroën garages at The Olympic in Amsterdam, tenants like the atmosphere, and want to be there because it is inspiring. Yes, we need more capex for the hardware. But don’t forget to pay attention to the software.”

### Life sciences boom

During covid, capital has poured into the life sciences sector. Last year, Blackstone raised \$7.5 billion for its life sciences office real estate perpetual fund and healthcare REIT Ventas formed a \$930 million joint venture with Singaporean sovereign wealth fund, GIC to develop life sciences space.

RoccoGrande quotes a statistic from another sector specialist, Alexandria

## Covid culture shock starts at home

### The participants share experiences of how their firms’ working practices have evolved during the pandemic

**Deacon:** In London we have 200 people and, up until covid, we were all pretty keen office users with a strong organizational culture. But when the pandemic hit, the decision was made pretty rapidly to send us all back home. There has been variation between Nuveen’s different national operations. In the US, very few people have been in the office. There has been modest uptake in London when we have been allowed back between national lockdowns, and much more in Amsterdam, Germany and Paris, where the teams are smaller, so there is a different dynamic.

**Jochims:** Our organization has about 200 full-time employees. At the moment, a maximum of 45 to 50 can come into the office. We see that particularly the younger people, most of whom live in Amsterdam, where our headquarters is, don’t have much space at home, and have children around, so we try to give them some comfort to come to the office. We are quite selective about who is able to go in. We see a lot of demand from our employees, though.

**Belford:** Last July, we shifted to an approach where people can go into the office voluntarily. We ended up finding that almost no one did, and we are still operating in that environment. Our attitude at first was “we have to get everybody back to the office as soon as it’s safe.” As we have gone on, we have shifted very significantly mentally to a new reality where, while the office will open back up, we think we will have to be very flexible with our employees for quite a while.

**RoccoGrande:** We have a lot of younger employees who use technology more and travel all the time. Some of our top performers do better when they are out of the office than when they are in it. Everyone is an adult and manager of their time, and I do not think that will change. The first part of this work from home experiment started off working wonderfully well. But today, I see less productivity from our teams, and part of that is due to lack of collaboration. I would guess the majority of our people would come back to the office straight away if they were allowed to.

*“The next 10 years will be dictated by where technology and artificial intelligence meet scientific research”*

FRANK ROCCOGRANDE  
Deutsche Finance International

REIT: there are 10,000 known human diseases, with only 500 effective treatments. “Do the math and tell me what the opportunity is there. If the last 10 years were about where the tech boom met consumerism, then the next 10 years will be dictated by where technology and artificial intelligence meet scientific research,” he predicts.

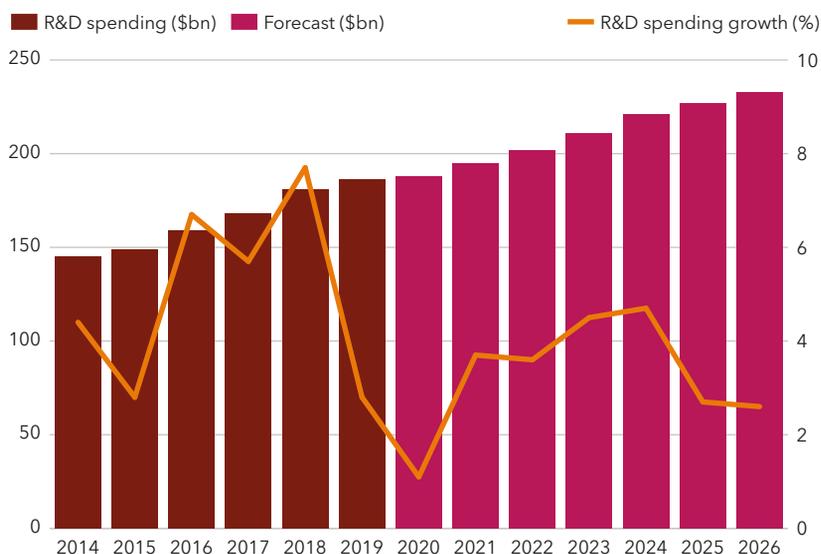
He notes that while covid has drawn attention to the sector, the real driver for the boom is evolution in the funding model for scientific research. “If you speak to any institutional investor and ask them to track their venture capital investments over the last decade, and how biotech is weighted in those allocations, it has gotten bigger and bigger.”

However, life sciences still represents a comparatively small segment of the office market and one with high barriers to entry. “There are players out there who have the advantage of really understanding the underlying industry and the companies in it. But they are relatively few. At the moment it is a challenge to access talent on the leasing and operational side,” says Belford.

Developing space in the few key life sciences clusters – Boston, the San Francisco Bay area, San Diego, the Netherlands, and the UK London-Cambridge-Oxford ‘golden triangle’ – can also be breathtakingly expensive, cautions RoccoGrande. “You need to invest 100 percent speculatively, and then sit down with the leading high-growth venture capital-backed firms in that region. Most investors don’t have the stomach for that, especially in Europe. We are a huge believer in growth in the sector. The challenge is going to be accessing product at pricing that makes sense.”

In many respects the life sciences segment encapsulates the themes of increased complexity and expense that are transforming the office sector as a whole. The pandemic has made it clear that the trend towards operational intensity that is unfolding across much of the real estate investment class, now unarguably applies to offices too. ■

Global biopharm R&D spend forecast to increase, generating demand for life sciences real estate (\$bn)



Source: Eavluate Pharma



“ It’s easy to manage a business from home, but it’s not so easy to build one ”

**Bas Jochims**, Director Dutch Office Fund, Bouwinvest

Brainstorming and innovation happen when we meet and inspire each other with ideas to make our businesses flourish. Video calls do not compete. Humans are social creatures. The real sparks will fly by the coffee machine in a post-Covid office, as safe as our own home, but more stimulating and flexible. Bouwinvest’s Dutch Office Fund is creating the working spaces of the future, ready for whatever time throws at us, because the only certainty is change. The expanding fund currently has investments of €1.2 billion in the new generation of sustainable people-friendly Dutch offices that are the only way forward for us and our investors.

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