

# Offices Are Changing; Investments, Too

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**T**he office sector represents the most significant portion of the asset allocation of institutional investors and the sector most influenced by the new modes of remote work. New work needs are thus leading to a change in demand for spaces and in the physical characteristics of new properties, but also in supply, with increasingly complex technological solutions and greater attention to services and the issue of environmental sustainability.

The pandemic has been an important accelerator of changes already underway in the office sector, with an unexpected acceleration of remote and agile working formulas. This has led operators, investors, and users above all, to question the relevance of this sector as regards investments, but especially to ask how it must adapt to change. Properties provide a service, so it is normal that the service must be adapted to the new needs of customers; but unlike others, the provision of the service depends on choices, location and quality of the buildings, which are difficult to change. By playing a central role in the life of workers, who spend most of their day there, and having a significant impact on emissions, offices also have a central role in Corporate Social Responsibility policies.

## THE TOP REAL ESTATE ASSET CLASS FOR INVESTMENT VOLUMES

If we analyze the data, we see that the office sector historically represents the most significant portion in the asset allocation of institutional investors, and the first half of 2022 is no different, with the service sector that represented approximately 39 percent of investments in commercial real estate at the European level and approximately 31 percent in Italy.<sup>1</sup>

These numbers are confirmed by Alexei Dal Pastro, according to whom: “In the first half of 2022, offices confirmed their role as the top asset class in the Italian real estate sector, growing more than twice

compared to the same period of 2021, with a take-up (new leases) in Milan at the pre-pandemic level, an increase in large office leases that shows significant dynamism on the part of large companies, that are gradually returning to the office.”

Analogously, according to Manfredi Catella: “Numerous studies confirm that the office sector is still one of the most important asset classes in the real estate market: there is a change in the criteria of choice, that are not dictated exclusively by economic factors, but above all those of quality, producing an acceleration of concentration of demand in integrated and connected neighborhoods. In recent years, for example, qualified neighborhoods in Milan and Rome have attracted 35 and 49 percent more absorption of space for office use, respectively, than in “undifferentiated” neighborhoods, and recorded greater growth of rents (9 and 14 percent, respectively).”

## REMOTE WORKING

The service sector, though, is the one which may be adopting the excesses of remote working in the most significant manner, in its various expressions, from home working to smart working. The common opinion is that this is not a temporary fad, but rather a true change in the way of working and using space.

According to Catella: “Already over a year ago, in the middle of the Covid-19 pandemic, based on two studies on the “Future of Offices” conducted with a

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group of companies with offices in Italy – in Milan in particular – it emerged that there is an increase of possibilities for employees to work remotely, yet without this phenomenon having a structural impact on the need for office space; rather, the likely reduction of the need for office space was relatively marginal, although not negligible, not entailing a deterioration of the sector for the future. The main conclusion that emerged from the investigations carried out was positive overall: a change in offices in the medium term, from places of production to places of interaction, with the consequent need to evolve to maximize the involvement and productivity of employees, stimulating their creative potential. This also strengthened the conviction of the need for growing interaction between companies, investors, developers, and architects, with greater attention to the relationship between space and experience, to create value from both a financial and social standpoint.”

The position of one of the main suppliers of co-working spaces is similar. According to Muhannad Al Salhi: “The pandemic has forced businesses to completely rethink their work strategies and adapt: teleworking had its advantages (flexibility, less movement), but it very quickly also showed its limits (work-life balance, isolation, IT security). As a consequence, the main trend today is the widespread adoption of hybrid work models and a clear orientation towards a future of more flexible work. Hybrid is certainly destined to remain, since it offers the best of both worlds (remote and office), while what is truly at stake is how to orient oneself between the two.”

“In a period of uncertainty,” continues Al Salhi, “companies seek first of all to reduce fixed costs and adapt to their needs. This means that flexibility of conditions and the possibility to rapidly increase (or decrease) space when and where necessary become fundamental factors. Flexible space (as well as distributed offices) are destined to become a broader part of their portfolios and access to shared spaces can be one of the most efficient workspace options that companies can take into consideration. “One-size-fits-all” in offices does not work for everyone, and as a consequence, the future is flexible. The pandemic created the opportunity to realign the misalignment between what the end user wants (employees, in this case) and what was available.”

Finally, according to Dal Pastro: “Smart working has changed the attitudes of workers, becoming an entirely new mode of work that will go well beyond the pandemic. A hybrid form is increasingly taking hold, that is emerging as a valid alternative between the definitive return to the office and home work, that allows for numerous advantages, including greater

balance between private and professional life, wellbeing, savings, sustainability, and attractiveness for talent. Yet there remains the need to confirm the long-term sustainability of that new approach to work, principally in terms of cohesion of the team, and as a consequence, of productivity.”

“Today,” continues Dal Pastro, “it is possible observe a gradual redesign of work environments to comply with the needs linked to hybrid work: this can lead to a reduction of the dimensions of spaces for some users, with the relative cost savings for organizations; but at the same time, it makes it necessary to configure them in a flexible manner, thinking of greater collaboration and interaction also outside of the pure work activities between those who populate them, without forgetting areas for privacy: more meeting tables, large monitors for sharing projects, digital signage solutions, relaxation zones and areas for stimulating creativity, devices for reserving workstations, and advanced videoconference systems to support the relations between people who work remotely and people in the office. At the same time, we also observe cases of increase of areas leased by other operators, who integrate the layout of offices with large spaces for collaboration and factorize a significant growth of personnel. In order for hybrid work to produce the desired results, it is essential to obtain the right tools, and in this case, technology is king: availability of documents in digital format, cloud information systems, collaborative platforms, continuous training, and all of the innovative tools useful to support organizations in this revolutionary transition from traditional work to hybrid work.”



### EVOLUTION OF DEMAND AND BUILDINGS

It is also interesting to understand how smart working and new work needs are leading to changes in the physical characteristics of new buildings, and where demand for space is actually changing.

According to Catella: “Given the possible aggregate reduction of the amount of leased office space, offices must reaffirm their role as centers of experiences. There are three factors that drive demand for these spaces today: position of the building, flexibility, and quality, while price comes in fourth. The need for sharing experiences also requires the creation of common spaces that make up for the reduction of spaces dedicated to desks. But what is even more important, is that today offices, like the neighborhoods in which they are inserted and with which they have a daily dialogue, must meet the most advanced standards of technological innovation and environmental sustainability, with particular attention to the reduction of emissions in respect for the EU 2050 decarbonization goals.”

“If we look at demand as a whole,” continues Catella, “the studies conducted indicate that approximately 50 percent of business will seek to reduce leased space, while the other half will preserve or increase office space. Within these parameters, demand is more polarized. The search by companies concentrates on neighborhoods having functions that are mixed, accessible and highly connected (i.e. reachable by public transportation), with public spaces and a high social dimension. Resilient, holistic, and high-quality neighborhoods, designed according to measurable Environmental, Social and Governance

(ESG) criteria, will attract demand from tenants who are increasingly sensitive to a broad number of aspects that go beyond price. Qualified neighborhoods will continue to benefit from healthy interest by companies that lease offices, while on the other hand, undifferentiated neighborhoods will very likely have to face greater difficulties, with a part of the office stock that risks remaining abandoned but that can represent an opportunity for reconversion to accessible residential.”

According to Dal Pastro: “The pandemic has acted as an accelerator of some dynamics already underway. We have seen a greater request for modern and flexible workspaces, with a component of service and technological innovation, and with facilities that favor inclusion, creativity, performance and efficient collaboration between people. Attention to the safety and wellbeing of users has become a priority, with buildings as flexible as possible in time and space and with a high “usage value.” It is important to take into account the evolution of tenant demand, considering many aspects: mobility, with a maximum distance of 10 minutes from public transportation, and where possible, smart mobility solutions to provide eco-compatible means of transport; permeability, i.e. buildings integrated into society, with spaces used also by people who live in the neighborhood, preserving privacy and safety; a high-level user experience that includes a broad range of services, spaces for collaboration, measures to safeguard the health and wellbeing of occupants and promote green areas; connectivity and innovation in the choice of materials, equipment, and digital technologies; and last, but not least, an environmental policy aligned with demand and corporate goals.”

### EVOLUTION OF SUPPLY

In recent years, however, we have seen not only the introduction of new modes of work, but also a different type of supply, such as that represented by co-working and temporary offices, that allow for obtaining greater flexibility in business spaces. In this case as well, though, the spread of these formulas, more than increasingly replacing traditional offices, represents for all purposes a complementary offer.

According to Al Sahli: “It is not about choosing between one (traditional offices) or another (co-working spaces), but it is clear that flexibility will win a larger market share. With the consolidation of hybrid working models, companies will increasingly seek to offer employees the possibility to choose when, where, and how to work, and this will often be a mix between home, central office, or third-party spaces. According to what is stated in the Flex Report 2021 by CBRE,



almost a quarter of the companies interviewed state that they have more than 10 percent of their real estate portfolio in flexible office spaces, while 24 percent of those interviewed anticipate that more than one-fourth of their offices will be flexible within the next two years. Today, flexible spaces represent 3 percent of the total surface area of offices, and it is expected this figure will reach 20-30 percent by 2030. Independent of terminology – “remote first,” “hybrid,” or “distributed” – there is a common characteristic that can be identified: companies want to see the future of work rooted in providing employees the maximum level of flexibility and possibility to choose. Nobody goes to the office anymore just because it’s an office. Flexible models of work have allowed people to be conscious of the reason they choose to go, and as a consequence, for businesses the possibility to offer employees the option to move to flexible and “turnkey” workspaces has become an absolute priority.”

Dal Pastro adds: “The flexible office will not substitute the classic office, but complete the offering. The real estate footprint of a company can be considered like a galaxy with a central planet, the office occupied with a traditional lease, and some satellite points occupied with flexible contracts. This system allows the company to adapt the available surface to its business activities, for example when new business lines are created or when there is a need to work on large projects, without being bound to a long-term contract. And offices are becoming increasingly strategic for some companies in terms of image or employer branding. For this reason, an office conceived as tailor-made, as a showcase of skills and business culture, will remain essential. And in this case, the possibility to have a long-term headquarters, designed ad hoc for the company, is essential. Our experience with the Wellio proworking format confirms this thesis.”

### THE IMPACT OF TECHNOLOGY

Whatever the type of offer, offices, like all properties, are increasingly technologically complex, and more than speaking of “brick and mortar,” today we would think of “hardware e software,” where the collection of data on the building and its use have become indispensable.

According to Catella: “Technology is considered an enabling factor for efficiency, services, and per-

formance of corporate offices, in particular in a scenario in which the greater adoption of remote work will see offices used more flexibly and will require greater coordination among employees. According to what is detected by the studies carried out, in response to the question relating to the technologies considered most interesting or useful to rationalize the use of office space, companies confirmed almost unanimously that they are interested in reservation systems, followed by tools that allow for monitoring the actual use of offices (in terms of both desks and overall space). Safety services enabled by technology and energy efficiency are in third and fourth place. More in general, technology is considered useful by companies also in relation to their ability to increase and improve the office experience. Lastly, it is evident

today that the possibility to gather data is becoming a fundamental variable, not only for the efficient management of individual offices.”

According to Dal Pastro: “The technology component already plays a fundamental role in the development of buildings and in their management. The curve of increase in the use of technology has been getting steeper and steeper in recent years, to the point of becoming almost vertical in the last decade. Artificial Intelligence (AI), machine learning,

and Internet of Things (IoT) are seeing large-scale expansion and in the near future will allow for much faster and more precise management of information. For example, consider BIM processes for the development of buildings and the management of these technologies (operation and maintenance). The use of those processes allows for much more precision and detail in controlling the resources deployed and more accurately evaluating the type and quality of spaces, as well as the needs of future tenants. BIM processes also help transmit to all stakeholders much more accurate information on the progress of the construction project, with the relative management of time, and on the final result of that process. Moreover, it is central in the management of the building, that thanks to BIM processes (and others as well) make use of a large volume of much more accurate, precise, and instantaneous information. The use of building management systems (BMS), in fact allows for gathering data directly in the field and in real-time, data that can then be remotized, so as to have more direct and detailed control for each building. The data refers to the use



of spaces, mechanical operations, electrical operations, etc. The collection and analysis of the same makes it possible to orient the management of the building and constitutes a rich database to be used to orient future developments, especially in terms of end user satisfaction. This de facto allows for a lengthening of the useful life of the building, thanks also to the promptness and precision of ordinary and extraordinary maintenance interventions, and the ability to adapt the use and comfort of the good in real time.”

These opinions are de facto confirmed by Al Salhi, according to whom: “This new world of work has created a propitious moment precisely because technology has a positive impact on the way people work. Companies must exploit a greater number of technological solutions to make the transition function and manage their teams on a daily basis. For example, the Access product, launched two years ago by WeWork, offers the possibility to access any WeWork workspace in the world through a telephone or by swiping a card. Through the Workplace service, companies and their employees can manage work hours and days in the office to collaborate, offering a universal system to manage their space. Moreover, the service allows for access and involvement of employees, who are involved in directly understanding what elements of buildings function well, and those that must be improved.

#### SUSTAINABILITY AND ESG CRITERIA

In conclusion, we cannot but focus attention on ESG themes, towards which the sensitivity of tenants and investors has increased strongly in recent years.

According to Dal Pasto: “The pandemic has gen-

erated greater sensitivity of demand to the risk of crisis caused by critical global events. This has given greater importance to aspects of environmental and social sustainability. Companies have reinforced their ESG strategies adopting an increasingly selective approach in the choice of properties based on criteria of sustainability, that does not regard only limiting environmental impact, but also care for the health and wellbeing of the human resources that populate those spaces. The spread of Leed, BREEAM, and Well certifications goes in this direction. Just consider that according to CBRE Research, the take-up of certified buildings went from 11 percent in 2016 to approximately 41 percent in 2021.”



percent of those interviewed), followed by waste recycling and the reduction of greenhouse gas emissions (with 76 and 74 percent), the promotion of greener transport options for employees (58 percent), and lastly involvement in the community (47 percent).

“Design complying with ESG criteria,” concludes Catella, “can play a crucial role in sustaining long-term growth, not only stimulating economies through investment, but also sustaining Europe’s global ESG initiatives. Lastly, it is essential to construct a more sustainable economy in line with the framework of the European Green Deal.”

<sup>1</sup> Source: BNP Paribas REIM.