

The Future of the Office: Not What You Might Think

While remote work has proliferated in a COVID-19 environment, we believe vibrant physical workplaces will remain in demand—and key to corporate culture.

Members of today's workforce likely never imagined that they would have to live—and work—through a pandemic. The lockdowns designed to slow the spread of COVID-19 spurred many companies to quickly leverage technology to shift their workforces to remote work. This experience has prompted a big question among industry observers: Will the quick fix of widespread working from home become a fixture over the longer term—and will it lead to a drop in demand for office space?

We believe the answer is no. In our view, successful companies value the power of in-person collaboration in shaping a dynamic corporate culture, and their employees do too. While remote work can be effective in the short and even medium term, it cannot replace human interaction forever, and it can introduce a long [list of risks](#). Ultimately, a company's culture needs in-person connection—and the physical workspaces that support it—to thrive.

Our outlook is based on our experience working closely with our tenants around the world, our observations in regions that have already started to recover—such as South Korea and Germany—and our history

as an owner-operator that dates back more than 100 years. With a portfolio of more than 250 office properties globally, we have managed through many challenging periods, including the dot-com bubble (when technological advances such as telecommuting were expected to render physical offices obsolete), the September 11, 2001 terrorist attacks, the Global Financial Crisis and the Brexit referendum. Offices endured these and other shocks, and we expect this resilience to continue through and after the pandemic.

An important distinction is that our view focuses on the area in which we own and operate office assets: the Class A segment—top-quality buildings in major urban centers with amenities catering to a “live, work, play” environment. We expect these assets will fare much better than older office properties with high levels of deferred capital expenditures or those in less desirable locations.

In fact, demand for high-quality office space may even increase in the long term as the psychological effect of the pandemic pulls back on the long-lived trend of office densification.

THE SHORT-TERM OUTLOOK: RESILIENCE

Throughout the pandemic, Brookfield's commercial properties, including offices, have remained largely open to enable tenants to maintain critical infrastructure and operations. Our primary focus is currently on helping our tenants implement back-to-operations best practices—and on communicating the steps we are taking to make our office properties safe for workers to return.

As part of this process, we have considered the potential short-term effects of the crisis on the office sector, surveying our tenants and seeing the implications play out firsthand. What we've found suggests that the sector impact in the near term will be limited.

Lease payments throughout the pandemic have been stable for high-quality office properties—in fact, our collections through June remained largely unaffected. Moreover, since office leases are long-term in nature (10 years or more), we believe the sector should be well protected against any short-term market downturn or negative sentiment that might arise over the next 12 to 18 months.

When it comes to working from home, we have seen employers take different approaches throughout this period. Some highly visible tech companies have announced that their employees will continue to work

remotely for an extended, or even indefinite, period. However, we remain skeptical that a significant number of tenants will end up with a truly remote workforce for any longer than they need to under their regions' reopening plans. Indeed, after having announced that up to half of its employees would work from home within the next 10 years, Facebook recently signed a lease for 730,000 square feet in Manhattan's West Side—in addition to another lease it signed late last year for 1.5 million square feet just a few blocks away.¹

The decisions by certain companies to keep their employees at home for the foreseeable future do not necessarily reflect long-term strategic shifts. In many cases, these companies cannot fit more than 50% of their workforce in the office while maintaining social distancing, and many government guidelines and plans have been in flux with uncertain timelines. Finally, it's worth pointing out that some tech companies are in the business of selling cloud services, online goods and apps, and therefore are in no rush to encourage their people to come back.

In the meantime, many of our own tenants are actively engaged in developing and executing return-to-office plans, the pace of which varies across regions. In many Asian countries, including China and South Korea, we have seen much of the workforce return to the office.

A BEST-CASE SCENARIO

South Korea has been highly regarded for its response to COVID-19 and its success in limiting the spread of the virus, and that success has extended to office properties. Most employees in the country have already returned to their workplaces. Indeed, our office towers in Seoul are approximately 90% occupied compared with pre-COVID levels. Workers throughout the country have willingly adopted health and safety protocols such as face masks and frequent hand washing and feel comfortable enough to take public transportation to work—a hurdle that has proven to be high in other regions. Despite the pandemic, we continue to see demand for high-quality office space and have maintained leasing activities. As a result, we are confident about the long-term prospects for the country's office sector.



- OCCUPANCY MAINTAINED OVER 90%
- IN Q2 2020, COMPLETED 107,000 SF OF NEW LEASING AND 48,000 SF OF RENEWALS
- IN PROGRESS WITH 15 NEW LEASES TOTALING OVER 162,000 SF

When employees return to the office, they will find that their environment has undergone significant changes. These may include heightened cleaning procedures in line with revised health guidelines, policies to ensure that sick employees do not come to the office, company-provided personal protective equipment and social distancing requirements. Employees may also notice new office layouts and upgraded features,

such as spaced-out workstations with transparent barriers, no-touch elevator systems and new air filtration systems to circulate cleaner air. In fact, at Brookfield, we are piloting advanced air ventilation and filtration systems in our New York, Toronto and Calgary offices, with an eye toward utilizing this technology in all our leased office properties.

THE LONG-TERM OUTLOOK: THE OFFICE, REAFFIRMED

Certainly, potential shifts in office demand will hinge on broader factors. Governments need to balance safety concerns with reopening goals, which will play a major role in determining corporate plans. The development of an effective vaccine or treatment for COVID-19 will, when it comes, also clearly be a game-changer in the evolution of the pandemic and its effects on employment.

Regardless, based on our investment experience across real estate markets, we already see some trends emerging over the longer term:

Working from home will ultimately become a supplement to, rather than a substitute for, the office. While remote work can provide flexibility for employees, office work allows for collaboration, connection and culture—essential ingredients for enterprise growth, risk management and control, and employee development. According to a recent [report](#) by the FICC Markets Standards Board, widely distributed remote workforces pose over 40 specific risks to companies, including those related to cybersecurity, confidentiality, execution, staff treatment and productivity.²

CULTURE SHOCK: THE ADVERSE EFFECTS OF WORKING FROM HOME, ACCORDING TO OUR TENANTS

While remote work can improve work/life balance among employees, extended periods at home can be detrimental. In a recent [report](#), the National Bureau of Economic Research found that work-from-home days are longer (by 49 minutes), with more meetings to attend and emails to answer.³ Working parents risk burnout from trying to balance work, home schooling and childcare. Loneliness can mount among singles and others who live alone. And beyond mental health risks, increased sedentary time can also take a toll on employees' physical health and well-being.

For companies, the negative effects of remote work over the long term can be stark, threatening not only their culture, but their very future.

Over the years, our tenants have consistently told us that junior to midlevel employees are the linchpin to getting the culture right (or wrong). These workers are not only a company's eventual leaders, they're key to innovation in the present, helping ensure that the firm can adapt and grow with the times.

As much as half of a company's workforce can consist of employees hired in the past five years. Retaining junior employees is challenging enough under normal circumstances—companies typically lose up to 15% of their workers to annual turnover, with a large portion being junior and midlevel employees.⁴ This is why successful companies invest heavily in recruiting, onboarding, training, mentoring and advancing these workers.

In a virtual environment, collaboration, ad-hoc interactions, personal attention and mentorship become much more difficult. And making newer hires feel invested in a company's future can be next to impossible.

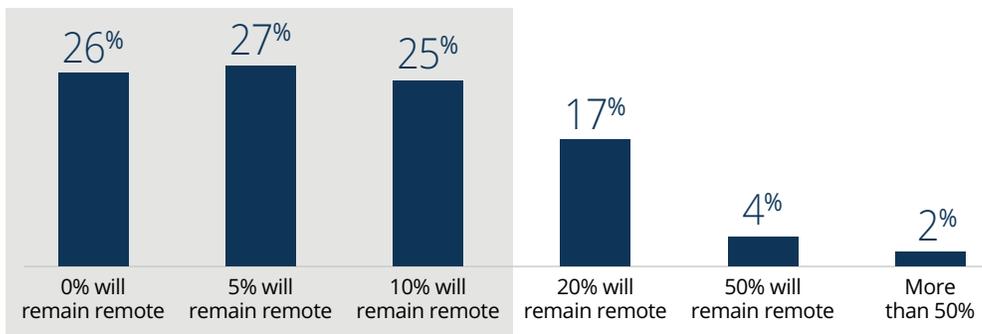
In-person interaction is particularly important when onboarding and mentoring younger employees—which, of course, are key to a company’s long-term growth. Our tenants tell us that these processes cannot be replicated and maintained through video conferencing over the long term.

It appears the tide may already be turning on the idea that working from home will last forever. According to the *Wall Street Journal*, more companies are now saying that they don’t see working from home as a long-term

solution.⁵ Barclays CEO Jes Staley recently commented on the importance of having workers in the office over the long term: "We want our people back together, to make sure we ensure the evolution of our culture and our controls, and I think that will happen over time."⁶ Indeed, most of our tenants tell us they are excited to get employees back in the office and interacting. A recent survey of over 2,300 workers in the U.S. shows that many employees feel the same way (see below).

WHAT PERCENTAGE OF YOUR WORKFORCE WILL REMAIN PERMANENTLY REMOTE POST-COVID-19 WHO WERE NOT REMOTE BEFORE COVID-19?

■ % of Companies



A RECENT SURVEY INDICATED 78% OF COMPANIES EXPECT THAT 10% OR LESS OF THEIR WORKFORCE WILL REMAIN PERMANENTLY REMOTE.

As of March 30, 2020. Source: A Gartner, Inc. survey of 317 CFOs and finance leaders.

DO YOU PREFER TO GO BACK TO THE OFFICE OR CONTINUE TO WORK REMOTELY?



ONLY 12% OF U.S. WORKERS WANT TO WORK FROM HOME FULL-TIME, ACCORDING TO A RECENT SURVEY.

Source: Gensler U.S. Work From Home Survey 2020. The survey was conducted online through an anonymous, panel-based survey of over 2,300 U.S.-based workers who were full-time employees of a company of 100+ people. Each respondent routinely worked within an office environment prior to COVID-19 and was currently working from home at the time when the survey was released between April 16 and May 4, 2020. Responses were evenly distributed across 10 industries and represent a wide range of seniority levels, roles, ages and geographies.

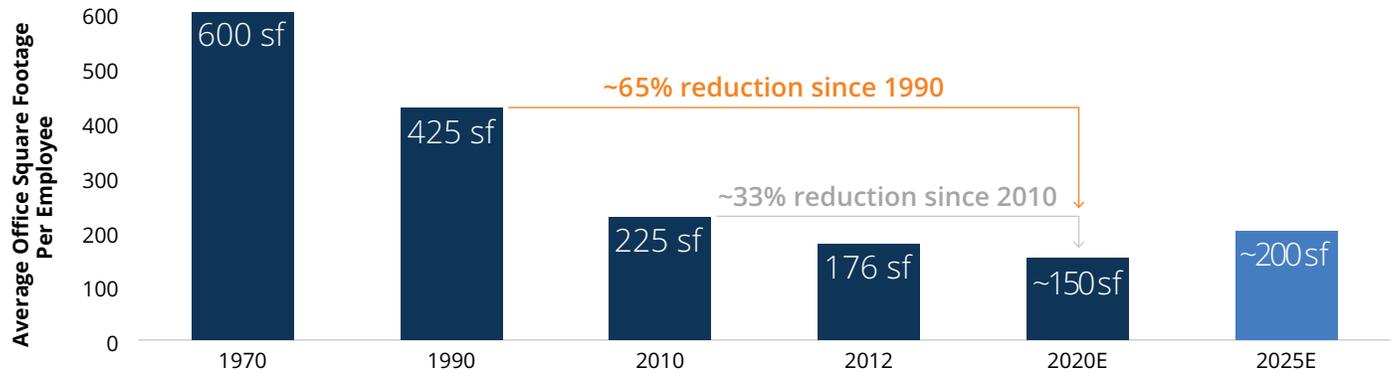
Square footage demand will remain stable—and in some cases may even increase. It’s a misconception that any permanent uptick in remote work will automatically result in a decrease in the amount of office space needed to accommodate employees. With virtually all employees coming into the office at least some of the time, companies will generally need at least the same amount of space as they did before the pandemic.

Most employees also want more personal space, not only for health and safety reasons, but because the decades-long move toward office densification may have swung the pendulum too far in one direction. For example, many workers will happily bid farewell to “hot desking,” the office trend that provided employees with a limited number of unassigned seats to share among themselves.

And with certain social distancing norms and health and safety protocols likely to endure, some employers may require even more space. Based on our research

and live examples, this could translate into around 200 square feet per person (about the average density seen in 2011) and a need for about 33% more space.

COVID-19 WILL LIKELY REVERSE THE OFFICE DENSIFICATION TREND

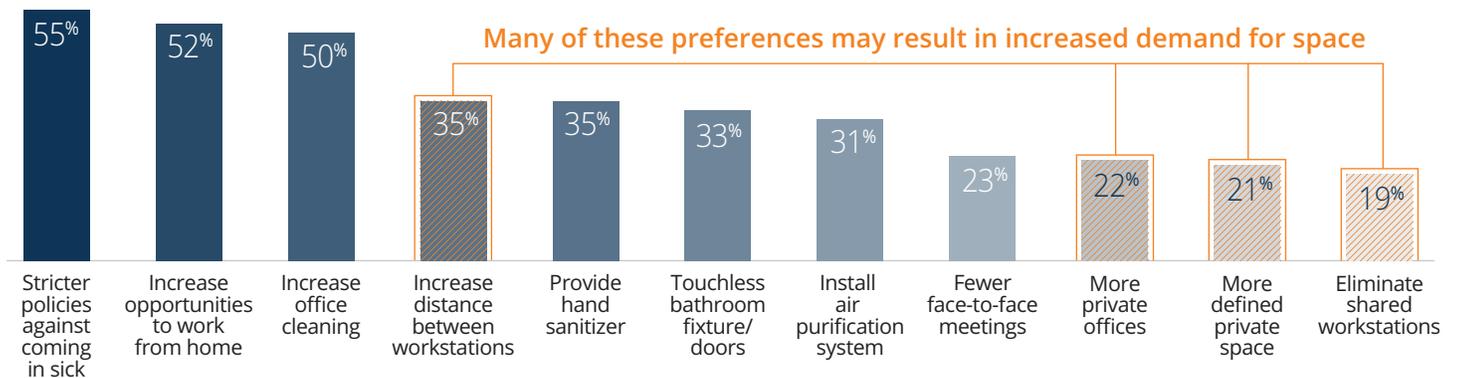


Source: UBS, Cushman & Wakefield, Brookfield Research

In our experience, some tenants have already begun to explore ways to reconfigure or even add space to their offices over the long term. Indeed, one of our tenants in Asia nearly doubled its office space just weeks into its country's lockdown. Companies with dense trading floors in particular will need to prioritize changes to those spaces, since trading jobs—more so than many others—require employees to be in the office. And, finally, some companies are looking to add space dedicated to hosting meetings with external clients, in some cases on self-contained floors.

We expect that a shift back toward providing employees with more personal space, perhaps closer to the average square footage per employee a decade ago, should prove to be durable even in a post-vaccine world as fears and social distancing expectations linger (see survey results below). In a recent report, UBS shared the same view, stating that “businesses are unlikely to want to go through the process of removing chairs as they are doing now, and instead move towards a more sustainable (i.e., lower density) set-up in case of a new pandemic.”⁷

WHICH CHANGES TO YOUR COMPANY'S OFFICE ENVIRONMENT WOULD MAKE YOU FEEL COMFORTABLE RETURNING TO THE OFFICE?



Source: Gensler U.S. Work From Home Survey 2020. The survey was conducted online through an anonymous, panel-based survey of over 2,300 U.S.-based workers who were full-time employees of a company of 100+ people. Each respondent routinely worked within an office environment prior to COVID-19 and was currently working from home at the time when the survey was released between April 16 and May 4, 2020. Responses were evenly distributed across 10 industries and represent a wide range of seniority levels, roles, ages and geographies.

Gateway markets will continue to attract and retain tenants. The death knell has been sounded for cities many times in the past—the future of New York alone was questioned by many during the fiscal crisis of the 1970s, the crime waves of the 1980s and 1990s, the aftermath of 9/11 and the Global Financial Crisis. Of course, New York not only weathered these storms but emerged stronger, for one simple reason: People young and old want to enjoy the vibrancy of a great city.

High-quality office spaces in leading, supply-constrained markets will also continue to draw tenants because major cities will continue to serve as magnets for talent. This, we expect, will remain the case even as we face the challenges of COVID-19—and is a reason why such assets represent a significant portion of our real estate portfolio.

Lower supply could offset a drop in demand for office space. In light of the pandemic and its chilling effect on investors' perception of office real estate, new groundbreakings are likely to be minimal, as construction lending inevitably tightens. A July 29th Citi Research report notes that the current level of U.S. office starts, as a percent of U.S. office stock, is meaningfully below the historical average.⁸ Less new construction could, in turn, put further upward pressure on demand.

Now doesn't mean forever. Our many years investing in real estate have taught us the value of maintaining a long-term perspective. After 9/11, for example, almost everyone expected companies to vacate higher office tower floors in droves, and it was difficult to imagine workers feeling comfortable returning to business as usual. But while the memories

THE MODERN OFFICE AFTER COVID-19

One of the many things that Brookfield's technology investment team thinks about is what the future might look like. The Silicon Valley-based group focuses on building a portfolio of attractive investments in growth-oriented businesses at the intersection of real assets and technology. Some of the emerging trends they're watching in the office space include:

- **Virtual marketing and leasing.** New full-suite commercial real estate marketing and listing platforms enable landlords to market and lease space remotely. As consumers and tenants become increasingly tech-forward, platforms like these allow tenants to experience and design a space virtually. This not only makes lead generation easier for landlords and brokers, but also appeals to smaller, tech-savvy tenants.
- **Space-utilization analytics.** Some landlords, facility managers and occupiers are using sensors and beacons for real-time data on how spaces are used—from determining the availability of specific meeting rooms for instant bookings to helping with anonymous people-counting and space density requirements amid COVID-19 or a future pandemic.
- **Robotics and the Internet of Things (IoT).** Autonomous robots are helping to clean and sanitize office environments overnight, providing employers and facility managers with a solution that minimizes human exposure in a workplace. These units are able to identify and classify physical objects around the office and provide data for record keeping and scheduling. Robotics are also starting to enable remote security checks, which could help minimize human interaction while also providing a human touch via a screen.
- **Air-quality improvements.** New technologies are emerging to ensure that the air workers breathe is safe. Before the pandemic hit, Brookfield began piloting a bipolar ionization system to improve air quality at our office properties. Instead of having air pass through a filter, this technology emits positively and negatively charged ions that can attract, bind and neutralize virus particles in the air. A bonus: These systems also reduce energy usage and emissions. Following third-party testing and validation of the pilot, we plan to roll out the system to all our office properties.

of that event have had an enduring impact, everyone eventually did get back to work, even on higher floors. At the same time, some new procedures implemented immediately after the attacks—such as security screenings and the use of ID cards—became permanent features of the commercial real estate landscape.

In that same vein, it's important to distinguish between temporary measures in the wake of the COVID-19 outbreak and longer-term practices. Even after a vaccine for COVID-19 is developed and implemented, many new cleaning regimens, floorplans and technologies will likely remain workplace fixtures. But we expect other hallmarks of this distinct point in time—such as workdays

in the home office revolving around a laptop and videoconferences—to have a much shorter shelf life.

Working with high-credit-quality tenants and maintaining an extended weighted-average lease term (WALT) in a portfolio can serve as a counterbalance against knee-jerk reactions. The original Brexit referendum in 2016, for example, did not have a significant impact on our London assets. Our leasing continued with no interruptions through headlines proclaiming the demise of London as a global business center. In fact, during that time, our office occupancy levels remained stable, and the city has only further solidified its leading role in the global economy since then.

THE BOTTOM LINE

There is no doubt that the pandemic experience will leave a lasting mark on people and how they live their daily lives. Governments will need to ensure that people feel safe taking public transportation again—and working in an office will need to be worth the trip. Before the lockdowns, office spaces were already a key factor influencing a company's ability to attract and retain the best and the brightest. This will only become more important in the post-COVID-19 era as the psychological effects of the pandemic potentially lead workers to seek out companies with more spacious layouts.

Ultimately, we expect the office sector to continue to thrive, with even greater demand for high-quality office buildings with the best systems, technology and sustainability credentials. These offices will be well-equipped to provide an environment that harnesses the power of in-person connections, along with added support for employees' health and safety. In other words, we believe that the new normal will look a lot like the old normal—and that the office will reemerge as the center of gravity for companies and their employees.

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Investors should consult with their advisors prior to making an investment in any fund or program, including a Brookfield-sponsored fund or program.

ENDNOTES

- ¹ New York Times, "Facebook Bets Big on Future of N.Y.C., and Offices, With New Lease," Aug. 3, 2020
- ² FMSB, Spotlight Review, "Examining remote working risks in FICC markets, July 2020
- ³ National Bureau of Economic Research, "Collaborating During Coronavirus: The Impact of COVID-19 on the Nature of Work," July 2020
- ⁴ Mercer, "North American Employee Turnover: Trends and Effects," January 29, 2020
- ⁵ Wall Street Journal, "Companies Start to Think Remote Work Isn't So Great After All," July 24, 2020
- ⁶ BBC, "Barclays: We want our people back in the office," July 29, 2020
- ⁷ UBS, Global Real Estate Analyser, "Special edition: COVID accelerating shifts in real estate landscape," June 29, 2020
- ⁸ Citi Research, "Shovels Down," July 29, 2020

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