Summary report

The future of office demand: Central London after Covid-19
Recovery and reimagination

The background
London’s urban economy and its office market have been among the most dynamic in the world in recent decades. But the Covid pandemic presents unprecedented and serious challenges for both.

In the wake of the outbreak, many offices closed, and working from home became mainstream. In the early stages of lockdown in March, some 78% of UK workers in professional, scientific and technical services were homeworking. By early September, this figure had fallen back somewhat - but still stood at 62%. Use of the tube rose from the ultra-low figures seen during lockdown to 43% of average levels in early September, but has since fallen back.

At the time of writing, an increase in Covid cases has led to further restrictions and a second lockdown. Government suggestions that people return to the office if they can have been reversed. Even if this is short-lived, it is evident that it will be some time before the threat of the pandemic subsides and the ‘new normal’ emerges.

The nature of that new normal is increasingly contested. At present, companies are focussed on cutting costs during the Covid-induced recession. Commuters are anxious about using public transport - a particular issue for Central London, given 90% of workers travel by tube or train. Many commentators are assuming these are signposts to the future, when in fact the real direction of travel will only be apparent when the pandemic subsides and companies start planning for growth and investment again - probably from the middle of 2021.

As recovery from the crisis takes hold it will become obvious that the trends that have made London a global hub have intensified. While networking technologies are here to stay, the unique productivity benefits of face-to-face contact and high quality office environments remain in place, as this paper will demonstrate. But London’s economy and its office market will have seen rapid structural change - much of it the result of an acceleration of the shifts JLL identified four years ago in Workspace, Reworked.

This paper examines the longer-term trends before returning to the question of how the market navigates the immediate challenges.

The market context
The office market in the UK capital entered the crisis in a strong position, with the volumes of both requirements and under offers above average levels.

At the end of June the amount of space under construction was half that recorded at the start of the Global Financial Crisis (GFC). Over half of that due to complete by the end of 2021 had already been pre-let.

However, Q2 and Q3 have seen some of the lowest leasing levels on record. Combined with the marketing of second-hand space, this has already pushed vacancy rates upwards. This looks set to continue as occupiers revise their requirements and more tenant-controlled space is brought to the market.

While the investment market has also seen a notable fall in activity, interest from investors has increased somewhat in recent months. It appears to be focussed on either prime or obviously value-add product.

Under offers and recent transactions have been stronger and Q4 should see a notable improvement on Q2 and Q3. This uptick is due to the higher risk-adjusted returns than in comparable global markets combined with London’s enduring attractions, including liquidity and transparency.

"Many positive views of homeworking are based on the experiences of established workers and teams, carrying out activities that were learnt in an office environment."
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Mapping the new normal

"More extensive homeworking will actually extend London’s commuter pull."
Homeworking

**Key market impact:**
Demand for high-quality offices remains robust, but more focussed on most accessible locations

**Key unknowns:**
Real scale of shift to homeworking over the cycle

The mass experiment in homeworking, made possible by high broadband speeds and video conferencing tools, has sparked a new debate about the future demand for offices. This discussion has focussed on the benefits and ease of remote working, but has often failed to highlight the productivity benefits of agglomeration. These may only be evident in the long-term, but are central to companies’ ability to innovate and grow, and are a key driver of London’s status as the most productive part of the UK economy.

It is too early to evaluate the impacts of homeworking and the implications of the experiences of the past few months for the future of the office. Many companies will no doubt experiment, particularly given the pressure on costs, but the ‘end state’ will depend on their experiences over a much longer period than the Covid pandemic has provided. As yet, there is little hard evidence on how productivity and both physical and mental health are affected, particularly in the long-term. Employment law in this area remains untested.

Many positive views of working from home (WFH) are based on experienced employees working in teams and on activities that had already been established in the office environment. There is already substantial evidence demonstrating how important face-to-face communication and collaboration is in business. The wider city cluster context, and the opportunities for both random and planned encounters with clients and competitors, are also hard to replicate online.

Soft factors are also important to some employees’ wellbeing and productivity, such as the social aspects of being in the office. JLL’s May 2020 Human Performance Survey, covering 3,000 employees, demonstrated that 58% missed their office a lot, with interaction with colleagues the most frequently selected reason.

There is increasing anecdotal evidence that companies are beginning to notice the downsides of remote working and are increasingly keen to encourage workers back to the office in some form.

Employees also appear to have an increasingly limited appetite for long-term, full-time homeworking – a recent internal survey by Google indicated that the number of staff wanting to work from home forever had halved between May and July, suggesting that the novelty may have quickly worn off and that many people continue to appreciate the benefits of working in an office environment.

JLL’s recent Human Performance Survey also showed that most employees want to work at home 1-2 days per week. Managing this flexibility, so that teams can collaborate where necessary, while preventing full occupancy on certain popular days (say Tuesday to Thursday) and much lower occupancy at other times, will be a significant challenge. There may also be different preferences by life stage and living arrangements, and ensuring everyone is comfortable with this will present a further issue. There is likely to be real variation by company and sector, and depending on perceived outcomes, some companies may insist on higher levels of attendance.

The implication is that, while homeworking will undoubtedly increase and the office market will see significant change, the ‘new normal’ may incorporate rather more elements of the ‘old normal’ than some of the media commentary has suggested. A new emphasis on location, quality of design and sustainability metrics such as net zero carbon will ensure that demand for the right type of offices remains robust over the cycle.

Office density

**Key market impact:**
Occupiers may require fewer desks, but more collaboration space

**Key unknowns:**
Whether companies can manage attendance over a week so that space savings are possible

The one trend that will reverse, certainly in the short-term, is office density. Since the early 1990s, space allocated per person has reduced by more than a third. Clearly, with re-entry, there will be far more space per person, although this is likely to unwind with time - but perhaps not to the levels seen pre-pandemic.

This will balance - but not remove - the potential reduced space take per company if homeworking becomes a significant part of employees’ lives. Our scenarios, as detailed in the main report imply an overall maximum change of between -28% and +13% depending on space density and the extent of off-site working. This may in practice be almost impossible for companies to smooth demand over the working week to achieve savings. These figures also reflect the changes for a single occupier; in the market, changed commuter patterns could lead to increased demand for a London base.
Office design

Key market impact:
Demand focused on high-quality, net zero carbon offices in attractive environments

Key unknowns:
Whether capex will be found to upgrade poorer quality space

The design of the office has changed considerably over the past decade. Hotdesking has led to a notable increase in employee densities in London, although this has been accompanied by the provision of more formal and informal collaboration space. Amenities and more thoughtful and inspiring design had become more critical, and occupiers had become more aware of the importance of the local area, recognising vibrancy and industry clustering could help their businesses.

Some of these trends will be accelerated by the pandemic. A mix of more homeworking and a more flexible approach to attendance will mean offices will have even more collaboration and meeting space and less formal desk space. The quality of fit-out, and the perceived sustainability and health & wellbeing qualities will become priorities. Rental profiles will polarise, with higher rents and lower yields for buildings that can cater to changing occupier requirements - and weaknesses elsewhere.

This will require space to be managed carefully. It will be difficult to avoid employees concentrating their visits on particular days, either to be with their team, or to be visible to senior management. Alternatively, parts of offices could be closed on ‘quiet days’.

A temporary weakness in office demand will allow landlords and developers to capitalise on value-add opportunities, including the introduction of smart technologies and improved sustainability. Occupiers are increasingly seeking space which is ready to occupy, as is common in some other countries, rather than functional but empty space ready to be fitted out by the occupier. In property jargon this is often referred to as Cat A+ and Cat B (varying levels of fit-out) as opposed to Cat A (simply raised floors, suspended ceilings and M&E services).

Maintaining local green space and leisure options will also be critical in ensuring buildings remain attractive. This may be more easily achieved on larger-scale campus developments where the landlords can subsidise struggling operators, but individual building owners could look to repurpose ground floors and public realm if appropriate.

While the virus remains a concern, occupiers may move towards buildings and fit-outs where social distancing protocols can be dialled up and dialled down as risk levels rise and fall.

Technology

Key market impact:
Smart technology becomes a key differentiator for buildings

Key unknowns:
Employee acceptance of some technologies

Mass homeworking has led to the widespread adoption of video conferencing applications such as Zoom, Microsoft Teams and WebEx. They will remain a key part of office life. There will be a focus on improving AV facilities and redesigning meeting rooms so that those dialling in do not feel as if they are ‘second class’ attendees.

The experience of Covid will lead to an acceleration in ‘proptech’ take-up - particularly in areas where occupiers want to improve the health & wellbeing credentials of their building, and with technologies such as digital office space management and touch-free entry systems.

Developers will realise more than ever that the next generation of offices will have to incorporate a range of these technologies in synchronised systems, leading to a new wave of genuinely smart buildings.

These technologies will also become more prevalent at both neighbourhood and city level, helping to understand and monitor pavement traffic and public transport passenger flows. This could reduce overcrowding and permit a data-driven post-Covid redesign of public and private spaces.
Commuting patterns

**Key market impact:**
Demand for offices around transport hubs increases

**Key unknowns:**
Changes in geography of skilled staff; impact of Elizabeth Line

More extensive homeworking will extend London’s commuter pull. If some workers only have to be in the office two or three days per week, for example, then they may be prepared to travel from further away. This would have two effects.

Firstly, existing London residents may opt to move out to suburban or rural locations. This could produce a temporary weakness in London residential pricing but may allow other sections of the workforce to move into or remain in Central or Inner London. In time, this would benefit London which had started to see lower levels of in-migration among twenty somethings; it would also benefit companies which were increasingly concerned about the housing difficulties of their younger staff.

Secondly, it would make a London-based job more plausible for a wider range of people. In particular, those living even further afield may be more willing to commute further if it were required less frequently, particularly if flexible season tickets are available. This would increase the demand for London offices, as more companies would feel it essential to have an accessible base. It is worth bearing in mind that nowhere in the UK is as accessible to as many people by public transport as Central London.

Combined with post-Covid sensitivities and changes in office design, this would have impacts on London’s economic geography. Demand may intensify for locations near overground stations and major transport hubs. Together with the emphasis on green space and health & wellbeing, this will benefit developments on the outer ring of Central London, such as Waterloo, Southbank, Paddington, King’s Cross/Euston and also the Northern City/Southern Shoreditch area around Liverpool Street, as well as stations along the Thameslink line.

Some more suburban London markets could also see an increase in demand. Local clubs or hubs - perhaps occupied on a flexible basis - may become more prevalent in popular suburbs. This applies equally to towns and neighbourhoods on the fringe of Greater London with excellent transport links, such as Croydon or along the Western Corridor. These could offer alternatives to the home for local residents on the days they are not travelling into London, but the viability will depend on the individual company’s resources and the distribution of their staff.
Getting to the new normal

Companies in London have faced a number of logistical challenges around how to safeguard staff who return to the office. The responses have included spacing out desks; working in mutually exclusive teams; and operating hotdesking on a daily basis. They may find themselves having to go through one or more cycles of reintroducing and then relaxing these measures - and their experiences are likely to impact on their longer-term strategies.

The more challenging barriers to re-entry relate to the wider London context, although with inventive thinking and private-public collaboration, they are not insurmountable.

Public transport

With some 90% of Central London commuters using the train and/or tube to get to work, the city is dependent like nowhere else in Britain on public transport. Many will be fearful about using them in the near-term. There are already signs of more people using the car to commute – if this trend continues it could lead to unprecedented congestion, pollution, and issues around parking in central areas. It is essential that the GLA, TfL and Central government work together to prevent this impacting adversely on London’s population and economy.

In the early stages of re-entry, rotating office occupancy will reduce overcrowding on public transport; as more workers come back, staggered start and end times could flatten peak loads. Flexible season tickets would encourage those commuting only a few days a week to use the train. Given superior ventilation and space on overground services, as well as potentially longer commutes, submarkets close to mainline stations may be more resilient in the medium-term.

Cycling and electric scooters

Cycling in London has become far more mainstream over recent years, and lockdown saw a further boom in usage. The government has also recently legalised electric scooter hire schemes, allowing them to operate in the capital. Dedicated and/or temporary cycling and scooter infrastructure will be essential if a wider range of people are to use these for mobility instead of the car or tube, helping office re-entry as well as reducing transport load and road congestion. Many boroughs have already begun investing, but the measures are sometimes controversial.

London’s demographics

Central London’s employees are significantly younger than those in the UK as a whole, with around half aged under 35. Given lower risks of serious illness, they are more likely to feel confident re-entering the office; indeed, their cramped and often shared home conditions may encourage them to do this. As they are more likely to live in Inner London, commuting - including cycling - will seem more viable. While London has seen lower levels of office re-occupation than some cities, this could lead to faster re-entry in 2021 as conditions change.

The importance of food and beverage

Supporting London’s food and beverage (F&B) and entertainment businesses will be vital to ensuring parts of the capital remain vibrant while social distancing measures are in operation – and beyond. They are key in attracting both employees and relocatees. Campus-type or large mixed-use schemes may benefit here, as they can support and curate businesses over this period in a way that is much more difficult in parts of the city with fragmented ownership. In London’s more established entertainment districts however, flexibility over licensing and alfresco drinking and dining will help maintain vibrancy.

Green and/or public space

Employees will seek green space near offices more than in the past – in the short-term, as an alternative to limited F&B options, and in the longer term, as health & wellbeing become ever more important. Buildings near high-quality green or public space will be in greater demand as a result.
Covid-19: The market impacts

**Short-term impacts**
- Recession and cost savings impact decision making & lead to more lease extensions & weaker short-term demand
- Ability to meet Covid protocols changes occupier preferences
- Fresh air and transport accessibility become key differentiators
- Yield gap with other European cities drives increasing investment in prime assets

**Long-term impacts**
- Demand for London offices remains robust as commuter pull increases
- Marked polarisation in yields, rents and lease terms between limited “post-Covid” office stock and remainder
- More of the offices sector becomes flex – operational assets with higher returns & risk
- Geography of office demand changes, with transport hubs & green space central

**Until Q1/Q2 2021**

**Q2 2021 to early 2022**

**2022 and beyond**

**Medium-term impacts**
- Occupiers seek high-quality buildings in which Covid measures can be dialled up or down
- Uncertain outlook drives greater use of temporary workers and flexible space
- Demand for “post-Covid” offices intensifies – driving new wave of value-add opportunities
- Increasing polarisation of rents and yields with interest focused on scarce high-quality product as supply of sub-optimal space increases

NB. Timeline is indicative rather than definitive, given risks around predicting post-Covid recovery.

**How the pandemic is changing office design**

**From the Covid office...**
- Emphasis on ventilation
- Lower employee densities
- Close to transport hubs
- Close to green space
- Contactless entry
- Flexible fit-out for Covid protocols

**To the post-Covid office**
- Net zero carbon
- Wellness and amenities
- Smart technologies
- Flexible fit-out
- Collaboration space takes centre stage
- Superb cycle storage facilities
- Integrated networking technology
Remote working will not lead to a fall in demand for high-quality offices in London over the cycle

Undoubtedly, the London office market is facing a difficult 12 months. Widespread working from home is causing many occupiers to reconsider their space requirements in the short-term and their space strategies in the longer term.

However, it is also evident that most companies do not see a future in which a significant portion of their workforce is 100% remote. Most employees want to be in the office for most of their working week. The ‘end state’ will depend on the experiences of companies and their interpretations of productivity - not just over the past few months, but into 2021. It is far too early to make sweeping statements about the likely balance of remote and office-based work over the 2020s.

The downsides of extensive remote working may not yet be apparent, while there are real logistical and management problems in ensuring that lower attendance leads to space savings. As companies and employees become more aware of these issues, the appetite for office attendance will increase.

On the other hand, for companies who do move towards a more remote model, a London presence may become more, rather than less, essential. As a result, demand for offices which offer the required post-Covid environment will remain robust over the coming cycle. This greater intensity of use also suggests that there is potential for prime rents to rise over the longer term.

Returns and risk become more polarised by geography and asset quality

This hybrid working model will lead to a shift in occupier requirements. Offices will need to be more spacious, with a greater emphasis on health & wellbeing; they will feature fewer - but larger - desks alongside a greater share of collaboration and meeting space; amenities and fit-out will be paid even more attention than pre-Covid; and investment in smart building technology and net zero carbon upgrades will accelerate.

Buildings with these attributes will see a rental and capital value premium; those without will struggle, without significant investment to bring them up to the post-Covid standard.

The geographic shifts resulting from more flexible working and the experience of the pandemic will also be important. Areas around stations with the highest connectivity to the wider UK (and beyond) may see increased levels of demand, and stronger rental growth reinforcing recent trends towards edge-of-centre campus or smaller mixed-use developments.

Proximity to green space, accessibility by bicycle, and an amenity offer that has remained vibrant despite the pandemic will also be vital. These factors will produce a more diverse rental and yield profile than has been typical in Central London in recent years.

Many office investments will become increasingly operational

This implies that the investment market will become more polarised over the next year and beyond, with a widening spread between a more narrowly defined core and a larger set of value-add opportunities.

Core properties will generally be those let on longer leases to corporates, with ‘state of the art’ fit-out and sustainability and health & wellbeing credentials, all aimed at propagating brand values and attracting staff. Given London’s relatively high yields, and falling returns in other assets, particularly fixed-income, demand for the relatively limited pool of core properties in London and other major cities could increase.

Beyond this core category, many assets will have to be refurbished and reorientated for a more flexible future. Many investors will have to accept a greater degree of management, curation and fit-out, and service service provision than in the past, as flexible leases become the norm. The start of this shift has already been evident, with many of the established REITs starting their own flexible space brands, offering more varied lease terms, and providing more active curation of space and tenants. In other words, parts of the market will become more ‘operational’ - more challenging in some ways, but, if managed well, potentially offering higher returns.

London and its office market is about to undergo a period of reinvention. Some of the changes that are underway - more cycling lanes or al fresco dining - may persist and make the city a more attractive place in the longer term. It may have less of a permanent pull for older, more established workers, but more of a pull for the younger and internationally mobile. The office may be a place for occasional meeting and collaboration for some in an organisation, and a second home for others.

The next few months will continue to provide some useful pointers, beyond those in this report, on exactly what this means for the office market of the 2020s. The factors that have made London one of the world’s most investible office markets may evolve somewhat, but the importance of talent and agglomeration will persist.

Implications for investors
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