U.S. OFFICE MARKET OVERVIEW: WHERE ARE WE AND WHERE ARE WE HEADED

By Mike Ebbitt

Developing and executing a strategic plan to help manage real estate and occupancy costs is an important consideration for businesses and firms. CPAs can assist their clients and employers in this decision by developing a budget and financial projections. A well thought out plan will have long-term financial implications and will impact the ability to attract and retain talent moving forward.

By sharing some examples of how other organizations are successfully using their space, this article offers valuable insights to develop your own occupancy strategies.

The U.S. office market is poised for moderate growth in 2019. Office-using employment is expected to grow by 1.5 percent or by more than 300,000 jobs – a modest deceleration from 2018, primarily due to a very tight labor market. Sunbelt and tech markets are expected to register the largest percentage gains in employment, led by San Francisco, Orlando, Houston, Austin and Tampa, each at 2.7 percent or more. San Francisco, Dallas/Ft. Worth, Houston, New York and Chicago are projected to add the largest number of jobs in 2019 – between 15,000 and 25,000 each.

Office-using employment growth, although at a slower rate due to labor market constraints, will drive further office market expansion in 2019. New office product will help meet strong tenant demand for modern, efficient, highly amenitized space to attract and retain employees in an increasingly competitive labor market. Occupiers will continue to seek flexible space offerings and lease structures that keep them adaptable to changes in the economy and their organizational needs.

Successful Strategies

With shorter business cycles and technological advancements and markets becoming more unpredictable than ever, occupiers will continue the shift to more flexible real estate strategies. Work environments and lease structures must be adaptable to support highly dynamic organizational objectives. Following are some growing trends.

1. The historically low levels of unemployment create some challenges for companies. Tenants are reevaluating their real estate as a result. The most successful companies are using their office space as an asset to attract top talent rather than merely an expense.
2. Another trend is the drive toward efficiency. For a growing number of office tenants signing new leases, workplace strategies are being used to optimize space needs. Nationally, the average range is 150-225 rentable square feet (RSF) per person.
3. Additionally, there has been a shift in the location of private offices. Companies are moving away from offices located at the exterior in lieu of designating their offices in the interior of the space. The main benefit is the addition of more natural light.

Tip: The first step toward effective space management is to gather and analyze demand forecast data at the business-unit level. Ideally, this should include the current state of seat occupancy and vacancy, as well as business unit growth projections.

4. Planning ahead. Use of forecast data is essential for making proactive real estate decisions. Effectively planning for future requirements necessitates more than that. It also requires buy-in and coordination between a company's leadership, HR, finance and real estate teams with the goal of minimizing the gap between space supply and demand to directly support business success. Working across business units in this way, executives can factor in long-term organizational needs, goals and planned projects to create fact-based strategies for future real estate needs.

Key takeaway: When done correctly, rather than merely reacting, an organization can proactively respond to changing business needs and priorities. The most common cost savings opportunities include reducing seat vacancy, trimming square footage, increasing space efficiency and tightening seat density.

Renew or Relocate Guide

Markets fluctuate, employees multiply and new technologies emerge. One thing is certain: you need to make room for the future even if you can't predict it. Whether that means a moderate renovation or full relocation, the following tips will help you start the discussion.

Size Matters. The size of your company will determine both the time the move will take and the type of lease terms you're likely to receive.

Whether it takes 12 weeks or 12 months, your move can be split into three phases: planning, selection and buildout.

Phase 1: Plan Your Strategy. Your move strategy is about more than picking a new building. A real estate decision can affect every facet of your business: productivity, revenue, well being, sustainability and future success. Questions to consider include:

- What are your company's broader business objectives?
- Which real estate decision will support those goals?
- How fast is your growth rate? Do you need flexible terms?
- What is your exit plan when the lease ends?
- Who is your workforce and what is their work style?

Understanding and acknowledging where your business is today – in terms of the demographics of its employees, their needs and wants, its operational processes, and leadership style – is the baseline for understanding what kind of space will best serve your business.

Identify inefficiencies in your current workspace, decide how the new space should function, present the plan to stakeholders and consider these questions:

- How can operations improve?
- What style of building suits you?
- Enclosed office or small cube?
- How many square feet per employee?

To gain feedback, use an executive questionnaire. Get insight from leadership on the scope of the project and the function of the space. Questions may include:

- Rate the quality of your existing floorplan. How do you define quality?
- What do you want to prioritize most? Customer image? Cost? Recruiting new talent?
- How important are informal meeting areas?

Time is your biggest asset. Procrastinating in Phase 1 is perhaps the biggest mistake you can make when considering a move.

Tip: It's never too early to start thinking about your occupancy plans. Kick off initial discussions no fewer than six to nine months before your lease expires.

Are renewals involved? Renewals without negotiations are dangerous. Why? Your landlord hopes he/she will not have to recapitalize your premises for another tenant. Revise your approach even if you plan to renew your lease. It is not a renewal, but rather "Building Option One" to compare with all the other buildings you will evaluate. In essence, your building provides you with two opportunities: the one your renewal option declares and the one you successfully negotiate using the open market as your backdrop of comparable spaces.

The fact is, you are considering leasing space in your landlord's building again, not simply renewing. As a result, all business points should be on the table for discussion.

Tip: Gain negotiating leverage by touring the market and understanding your options. Your landlord will work hard not to lose you.

Phase 2: Selection. Negotiate your lease. It is crucial that you understand all of the costs and risks associated with each property along with the terms to which you're agreeing. Insist on future protection clause in case your needs change. Perform proper physical due diligence so you're not surprised by building issues later.

Dangers to avoid in phase 2 include not thoroughly inspecting a building. Many tenants overlook one of the biggest liabilities in a new lease: the base building systems and condition of the premises; i.e., the physical condition and safety of the building. Poor infrastructure is an obvious red flag, but building enhancements can be just as concerning. When a landlord makes a significant improvement to the building (such as adding a new roof or replacing the HVAC), those associated costs are often billed back to tenants over the duration of the lease.

Tip: A proper inspection and lease protection can prevent a large liability from a capital improvement project.

Phase 3: Build Out. Begin coordinating your move during construction, up to 24 weeks before your move-in date. The steps include: select architect, design, city review, preconstruction and construction, furniture selection, information services and audio visual, security, signage, move-in.

Your plan should include:

- Initial planning: define roles, resources, budget, timing, change messaging and vendors;
- Communicate: prepare employee welcome materials and move instructions;
- Transfer: finalize security, mail and technology moves;
- Organize: label day 1 tasks, directions, workstations, keys and layout;
- Confirm: check inventory, end of lease terms, final invoices and do a walk-through of your old space.

Trend to Watch in 2019 – 'Open Office' Concept

More and more companies are closing the door on the popular "open office" design trend. A recent study shows that the open office may do more harm than good. Here are some thoughts based on science. The *Journal of Environmental Psychology* jumped into the fray and came out with a huge study (40k+ workers and over 300 companies). What did they find?

- Closed offices outperformed open offices for productivity;
- Proxemics issues (how people feel when close) create uncomfortable workers (and therefore less productivity);
- Noise and visual disruption (or as Geoffrey James says "visual and noise pollution") creates distraction and focus issues.

If your firm or company wants to give its employees space to collaborate and socialize without falling victim to these issues, new and emerging design trends may have the answer. Some offices incorporate the best of both worlds with flexible design plans.

Flexible plans offer private spaces for those who need a little solitude to get the job done – individual offices or small conference areas for groups to gather away from the crowd, but their main work areas still reflect an open design. People can sit among their peers in an open space for a few hours before moving to a private office to make phone calls or zone in on the details of a creative project.

Final Thoughts

The integration of these strategies, location factors and space considerations requires comprehensive due diligence and a measured approach.

The information provided in this article should help serve as a reference. While it can't replace the personalized insight gained from working one-on-one with a tenant advisor, it can offer a starting point for the considerations and steps that should be taken to ensure your facility is an asset, not just office space. ■

About the Author:

As director of the office tenant representation team based in DFW, Mike Ebbitt oversees the building and growth of the specialty group. His team assists tenants with occupancy needs in office properties throughout DFW and across the nation. Whether the assignment is a relocation, expansion, consolidation, sublease, acquisition or disposition, Lee provides end-to-end occupier representation services. Ebbitt may be contacted at mebbitt@lee-associates.com or 972-934-4004.