THE BOND BUYER

Will remote work change central business districts?

By

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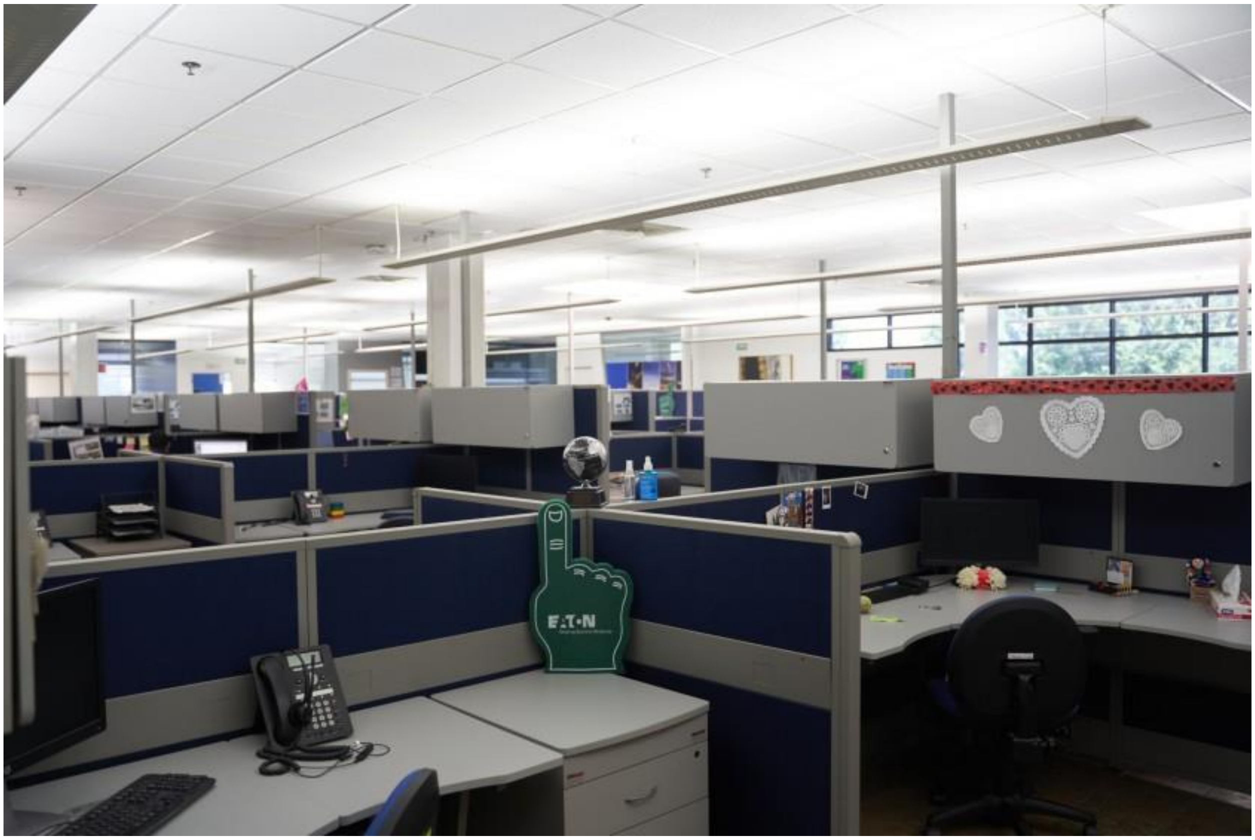
This article is part of The Bond Buyer's multi-platform, four-part series on the Future of Cities, each segment focusing on a different aspect of how life in and the finances of America's cities could be altered in the wake of the coronavirus pandemic.

We explore how cities of all sizes are being impacted by outmigration, and where the greatest long-term risks lie; the hard realities and intangibles of the so-called gathering economy – conventions, conferences, theater, sports and arts; how many businesses are at an inflection point with urban office space; and problems that lie ahead and how resilience has taken on a new meaning.

For each, we dig in on the problems and discuss potential solutions with a written story and a companion podcast. Additionally, the series features a video discussion spanning all four topics. To see all of our Future of Cities content, please click here.

The COVID-19 pandemic has reshaped life across America's cities. For employers, particularly those with expensive leases for space in skyscrapers in downtown business districts, it's become an inflection point to assess their future needs.

The open-ended work-from-home orders millions of Americans received from their employers, and the apparent success of that model to date, raise questions about the future commitment of corporations to basing their employees in cities or office buildings in general, and whether the work-from-home strategy can be a win-win situation.



Many offices remain vacant as companies figure out how to keep employees safe in what had been crowded workspaces.

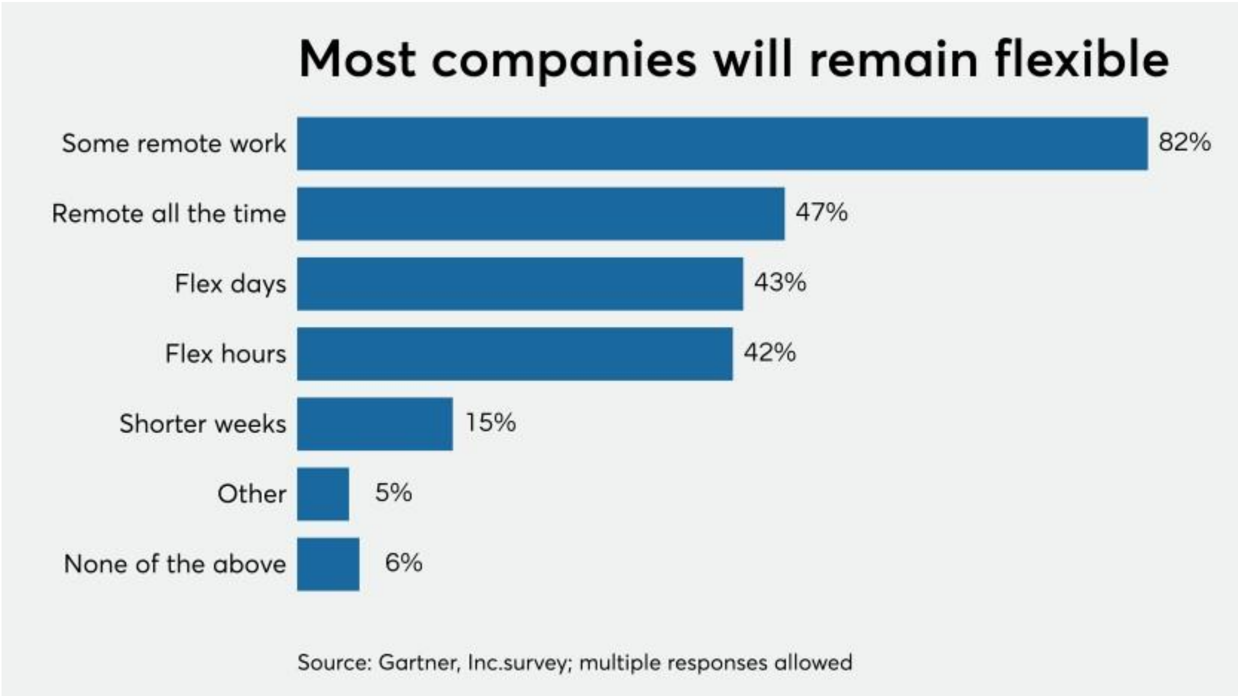
Bloomberg News

While businesses would reap savings from leasing smaller workspaces with most, if not all, employees working remotely, there are tradeoffs for businesses that can be more subtle to assess.

The resulting revenue drops from tolls, transit fares, sales taxes, parking meters, hotel occupancy taxes, and other fees have walloped the budgets of cities, counties, towns, and villages. There are also losses caused by employees not spending in central business districts, and, in turn, jobs lost in restaurants and other services in those locations.

But are these revenue shortfalls only temporary? Will these knowledge workers return to their central business districts when an effective vaccine is widely distributed? What percentage of workers will not return to full-time commuting?

The questions directly involve the one-third to 40% of the workforce that can successfully work remotely, according to experts. A June survey of 127 company leaders by the consulting firm Gartner Inc. found 82% intend to permit remote working at least some of the time after employees return to the workplace, and 47% intend to allow employees to work remotely full time.



Even before the pandemic, urban economists and planners were pointing to a trend of suburbanization of job growth.

The pandemic adds a layer of uncertainty over whether that trend will accelerate, as evidenced by highly publicized announcements from technology giants, such as Google and Facebook, that their employees who can work remotely will be allowed to continue doing so at least until 2021. In addition, Twitter has said its employees can do so on a permanent basis.

At the National League of Cities, Brooks Rainwater, senior executive and director of the Center for City Solutions, said cities have survived pandemics around the world and come out just as strong.

“They are still the centers for commerce and culture, and places where people want to live, work, trade, love and just enjoy the urban space,” he said. “In the short term, there’s going to be challenges and we already are seeing them arise.”

It’s still unclear whether the high-tech firms will maintain the same compensation levels for employees who move away from expensive locations such as Silicon Valley or the San Francisco Bay area, he noted. “Are they going to pay people the same salaries regardless of where they live?”

Consultants in the tech industry said the trade-off for employees engaged in remote work could go beyond the loss of onsite benefits, such as subsidized meals and worksite gyms. VMware asked employees who decided to move to

Denver from its Palo Alto, California, headquarters to accept an 18% salary cut, Bloomberg News recently reported, and those relocating to San Diego were asked to accept an 8% pay reduction.

Cloud-software maker ServiceNow Inc. is considering pay reductions starting in 2021 for employees who move out of the Bay Area, Bloomberg said. Facebook and Twitter are considering similar moves.

There are strong economic benefits to companies from telework as well.

If all federal employees eligible for telework did so half the time, the federal government could reduce its need for office space by 25%. Taxpayers would save $1.75 billion in real estate costs and $11 billion overall, the consulting firm Global Workplace Analytics estimated. In addition, federal workers would save on personal costs such as commuting, eating out and dry cleaning. The same type of savings can be assumed for private companies.

A recent Senate committee hearing examined how the benefits of telework in the private sector might be applied to the federal government.

Dell Technologies estimates it can reduce its real estate costs 20% to 30% over the next five years, Mark Pringle, senior vice president of corporate real estate, global facilities and environment, health, and safety told the Senate committee.

Dell already had 65% of its workers with flexible work arrangements prior to the pandemic and overnight increased that to 90%.

Pringle said an employee survey found 60% of Dell employees desire to work from home with the flexibility to go into the office for collaboration and meetings a few days a week. Twenty to 30% of employees want to work from home full time. And only 10% to 20% of employees would like to work in the office full time.

City magnetism

On the other hand, Facebook’s Aug. 3 announcement that it has reached an agreement with Vornado Realty Trust to lease 730,000 square feet in Midtown Manhattan provided more recent evidence of the draw of cities. Facebook will be a tenant in the former Farley Post Office, where the ground floor and underground area is being rehabilitated as the expanded Penn Station rail hub.

NLC's Rainwater pointed to the Facebook announcement as an encouraging sign for metropolitan areas.

Richard Florida, whose 2002 book “The Rise of the Creative Class” presciently predicted cities would thrive in the coming years as meccas for young tech workers and other creative people, doubled down recently on the forecast he made 18 years ago.

In a recent webcast by the University of Toronto Rotman School of Management, where he is a professor of economic analysis and policy, Florida described as "nonsense" any prediction the pandemic will lead to the end of cities.

Over the last two decades, for example, New York City has survived the Sept. 11 terrorist attacks, Superstorm Sandy and the financial crisis that led to the Great Recession, Florida said.

"I am coming to the point where I think it will strengthen cities," he said in reference to the pandemic. Cities, he believes, serve as a place for younger workers to develop a personal network. "It's very hard to do that remotely," he said. "That, and I can tell you a lot of people, almost to a person, they told me all of their job promotions have come from a personal contact, not from a virtual contact."

Urban economy experts have long pointed out the diverging paths of the largest thriving mega-cities, such as New York and Los Angeles, and the so-called second-tier cities, such as Detroit and Baltimore, that lost population in the last decade.

Christopher Berry, professor of public policy and director of the Center for Municipal Finance at the University of Chicago Harris School of Public Policy, shared the same mixture of optimism and concern in an interview with The Bond Buyer.

“My guess is, that within some finite, foreseeable period of time, people will be back to work and the advantages that cities have had will still be there,” said Christopher Berry, professor of public policy and director of the Center for Municipal Finance at the University of Chicago Harris School of Public Policy.

“My guess is, that within some finite, foreseeable period of time, people will be back to work and the advantages that cities have had will still be there,” said Berry.

The concept of cities where “ideas are in the air” goes back to the 19th century British economist Alfred Marshall, he said. “People just interact in unplanned ways,” Berry added, citing the rise of Silicon Valley. “That’s the whole logic for the innovativeness of cities.”

Remote productivity

However, Berry acknowledged the pandemic also has demonstrated to corporations their employees can be productive working from home.

“This is new information, new learning for companies, and that might lead them to decide, let’s just leave people at home after the pandemic,” he said. “And then why would they pay for all of this office space in cities?”

That sort of analysis only takes into account the short run. “People right now, as they work from home, are leveraging all the relationships and institutional knowledge they built up over a long period of working together in person,” Berry said. “So it’s much easier to maintain that productivity, at least for some period of time, after you have all this institutional capital built up through the in-person relationships.”

The question employers should be asking, according to Berry, is whether new hires will be able to be as productive. “That’s probably a question a lot of companies can’t answer because there’s not a lot of new hiring going on.”

The future

Gad Levanon, vice president for labor markets at The Conference Board in New York City, predicts a mix of responses by corporations to the pandemic, with the net effect of fewer people working in central cities.

“In some cases, there will be very little change,” he said. “For other companies, I think they will keep their headquarters in city centers but reduce their footprint because they will allow more people to work from home, entirely work from home or come to the office fewer days every week. So that would lower the demand for office space in the city center. And some may choose to leave the city center altogether.”

University of Chicago’s Berry said that after office space becomes vacant and commercial rents drop in the short run, there eventually will be a new equilibrium that lures other tenants because of the cheaper cost.

Joanna Ganning, an associate dean at the Maxine Goodman Levin College of Urban Affairs at Cleveland State University, thinks corporate headquarters will be increasingly drawn to cities because massive changes in the economy caused by the pandemic will require innovation, which is best fueled from face-to-face communication.

“It is part of an arc of a much bigger conversation about the relationship between technology and cities," said Joanna Ganning, an associate dean at the Maxine Goodman Levin College of Urban Affairs at Cleveland State University.

“We’re in the middle of a very dramatic episode in modern history,” she said. “It is part of an arc of a much bigger conversation about the relationship between technology and cities. At the end of the day, technology has changed cities, but it can’t erase geography. And there is evidence and theorists who will argue compellingly that the more important technology becomes to an economy, simultaneously the more important density becomes.”

People working together accelerates the advancement of technology, Ganning said. “We need people to innovate,” she said. “We need people to come up with a new application for it, and to do that, you have to be around people. It is part of social learning and the theory of knowledge network.”

Karen Lightman, executive director of Metro21 Smart Cities Institute at Carnegie Mellon University, made the same point.

“When you are coming up with novel new technology, there’s something about whiteboarding in a room with food that you are sharing,” she said. “There is something about that energy and that trust that you cannot build over Zoom.”

However, the central business districts of growing cities like Dallas and Charlotte, North Carolina, also have benefitted from growth of jobs and development of corporate headquarters in suburban areas. Their central cities have grown at a slower rate than their fast-growing suburbs.

The story is different for around 80 shrinking cities, such as Detroit, Buffalo, Cleveland, and St. Louis, where the region as a whole is growing only slightly, or contracting. In those places, the city core generally has suffered disproportionate job losses.

“There is not a clean-cut, one-size-fits-all answer here,” Ganning said, but overall the suburbanization of the economy is the single largest threat to city centers.

Carnegie Mellon's Lightman said it’s too early to tell whether corporations will relocate offices. But she has seen anecdotal examples of private citizens making their own decisions to move to the suburbs of Pittsburgh.

“I think when kids graduate high school, eventually they are going to come back to the city,” she said.

The NLC's Rainwater said one possible positive impact could be the movement of remote workers from the most expensive cities to smaller cities. “One of the challenges we have seen over the last few decades as a nation is the concentration of wealth in fewer and fewer places in America,” he said. “If there’s a way to grow back a stronger economy …. a bit more broadly in the country, that would be a net positive.”

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