Global Research | April 20, 2020

COVID-19
Global Real Estate Implications
Paper II

Contents

Executive summary

The COVID-19 pandemic has had a sudden and significant impact on all aspects of people's lives with 2.6 billion across the world now living under some sort of lockdown quarantine.[1] While JLL teams across the globe continue to monitor the situation on the ground and to support our clients through these challenging times, our regional and global research experts share their latest view on the implications of COVID-19 [2]. In this second paper, we assess what now happens as economies start to move out of lockdown, businesses begin the journey to 're-entry' and the real estate industry adjusts to a 'new normal'.

Impact on the global economy

Global economic growth came to an abrupt halt in Q1; the first global quarterly contraction since 2011. While different parts of the world are at different stages of dealing with the pandemic, all global regions have seen a severe slowdown. There continues to be a high degree of uncertainty for the outlook in a very fast changing environment. A V-shaped recovery is seeming less likely, and JLL recommends taking a scenario planning approach while maintaining agility and preparedness.

Global policy response to COVID-19

The COVID-19 pandemic, first and foremost, demands a health policy response. Along with health policies, governments around the world have also applied various social, monetary and fiscal policies to help support people, companies and economies. In the real estate sector, policies vary by country but include moratoriums on evictions, mortgage holidays and retailer tax reliefs.

Are green shoots emerging in China?

China was the first market majorly impacted by COVID-19, causing unprecedented restrictions on mobility. Two months after the introduction of these measures, China is now starting to loosen lockdown measures, and many traditional industries are slowly returning to normal. At the same time, others are seizing emerging growth opportunities with potential positive impacts for real estate markets. These include the digital economy, online entertainment, insurance, healthcare, and real estate technology.

Re-entry: Operational resilience and the 'new normal'

Businesses will not go back to the way we knew before the pandemic, but will use this crisis to reinvent themselves to be more resilient, adapting their operational models to the 'new normal'. There are four stages for corporates to transition through: prepare, respond, re-entry and reimagine. The re-entry stage focuses on the workforce, people and asset protection, along with workstyle adaptations. The impact of policy and decision-making will greatly influence the path for re-entry and force corporates to constantly adapt.

Real estate capital markets

Over the short term, investment activity is expected to slow as valuation challenges and broader uncertainty create barriers to investors' ability to appropriately price risk. Defensive sectors such as healthcare and logistics assets continue to garner interest as active investors consider income stability, operation criticality and occupational density to be key factors in mitigating asset-level risk. Despite ample liquidity across debt and equity, lenders and investor alike remain in a phase of 'price discovery' and asset management. Regardless of fluctuations in sentiment and activity, the overall trend has been for higher allocations to real estate, and we see no reason for this trend to reverse over the medium to long term given the advantages of real estate investments.

A catalyst for change: potential sectoral implications

The way we are all currently living and working differs vastly from this time last year – those changes that will become part of our 'new normal' following the relaxation of the lockdowns remain to be seen. This latest report explores some of the emerging structural trends by property sector.

[1] World Economic Forum, April 9, 2020

[2] COVID-19: Global Real Estate Implications, JLL, March 12, 2020

Offices

In the short term the flexible space sector is likely to undergo significant consolidation, although in the longer run it will remain a key feature of global office markets. Despite the current switch to mass remote working, the physical office will maintain its importance for facilitating interaction and collaboration and, ultimately, for employee health, well-being and productivity.

Retail

For retailers, the primary focus in the near term will stay on preserving cash. However, as the structural change in the retail market accelerates, greater emphasis will be placed on the shift toward a flexible omni-channel retail model and sustainable fulfilment.

Logistics

The COVID-19 pandemic will force operators to concentrate on supply chain risk mitigation and resilience. It will accelerate trends already in evidence across the sector prior to the pandemic: increased online penetration rates, expansion of online grocery, omni-channel retailing and the integration of technology into warehousing.

Hospitality

International travel around the world has ground to a complete halt, directly impacting the hotel market. Once the industry starts to recover, the destinations and types of lodging preferred may change. Domestic, driveable locations may grow in importance, while professionally-run lodging may have a greater appeal due to higher enforceable hygiene standards.

Living

The living sectors are generally viewed to be more resilient in the face of a downturn; however, the different sub-sectors have very different characteristics. Multifamily is usually considered to be the most resilient sector and this is being supported, at least in the short term, by various income-protection schemes. A decline in international student intakes poses a risk to the student housing market come the Autumn / Fall semester. While health care remains in demand, it continues to be on the front line of the pandemic. In the coliving sector, platforms that derive more income from corporate workers and longer-term residents are better protected than those oriented toward more mobile, short-term residents.

Looking beyond the pandemic

Overall, the way we live and work is changing, and some of the emerging new trends will become part of the 'new normal'. At the same time, many of the familiar pre-COVID-19 structural trends will be reinforced and will continue to shape the real estate sector. These include growth in corporate outsourcing, rising capital allocations to real estate, urbanization, technology and sustainability.

Setting the scene

The COVID-19 pandemic is now a truly global phenomenon with 2.6 billion people (a third of the world's population) now living under some sort of lockdown quarantine.[1] The short-term human and economic impact is undeniable as people stay home, offices and shops close, and production stalls. Once the risk to human life has reduced and steps are taken back toward a fully productive economy, it is worth spending some time envisaging what this 'new normal' might look like. China is offering us some visibility on what this might be.

The level of uncertainty in the economy is currently at an all-time high with the trajectory of the recovery difficult to forecast. Although there has been no global joined-up policy response, individual countries have taken major steps to try to cushion their people and economies through this difficult period. We look to the economic outlook and policy steps, but would advise against putting too much weight on a specific-point forecast until the future pathway becomes clearer.

In the real estate sector, we can see that the pandemic has accelerated some trends already in evidence, whereas other trends may reverse. For example, demand for online shopping has increased and will likely continue, while the ongoing trend for the densification of work and living space is now under scrutiny. Across sectors these trends differ and have varied implications for real estate demand. We examine each sector to see what their future characteristics may look like.

For our clients we continue to monitor the rapidly evolving situation and have compiled an assessment of the longer-term structural changes that may come out of the pandemic, as well as an economic update and some thoughts on what our 'new normal' might be.

[1] World Economic Forum, April 9, 2020

Impact on the global economy

Pandemic alters economic growth expectations

Global growth grinding to a halt
Global economic growth likely came to an abrupt halt in Q1. If so, it would mark the first quarter of contraction in the global economy in 11 years, since the end of the Global Financial Crisis (GFC). Strong involuntary measures implemented to combat the coronavirus outbreak, plus voluntary reductions in economic activity, have severely impaired economic activity.

Elevated levels of uncertainty combined with fast changing data have diminished the reliability of forecasting in the near term. Nonetheless, growth in 2020 looks set to contract for the first time since 2009. The path forward should become clearer throughout the second quarter with more data on both the trajectory of the pandemic and the state of the global economy.

Regional views
Though data indicates that countries around the world are undergoing similar experiences, the exact timing and magnitude will differ. In Asia, where the outbreak occurred earliest, some countries are further along in containing the outbreak and bringing their economies back online. In China, which introduced an early and strong lockdown, the economy continues to slowly and cautiously reopen. Though the risk of the outbreak re-emerging remains, a cautious restart in China provides hope of a sequential recovery in the rest of Asia.

In Europe, though the outbreak generally happened later than in Asia, the implementation of lockdowns brought similar negative consequences for economies. Data through February shows limited impact on major Eurozone economies such as Germany and France, as well as the U.K. But readings from March reflect a sudden impact to both the services and industrial sectors. For Europe, the most severe effects will probably lie during the second quarter before stabilizing toward the end of the year.

In the U.S., the response to the pandemic lagged Europe by several weeks, but lockdowns of citizens and shutdowns of businesses produced the same result. Data released from mid-March shows an economy seizing up and operating well below capacity. The economy will likely face an unprecedented contraction during the second quarter, potentially lingering into the third quarter before steadying toward the end of the year.

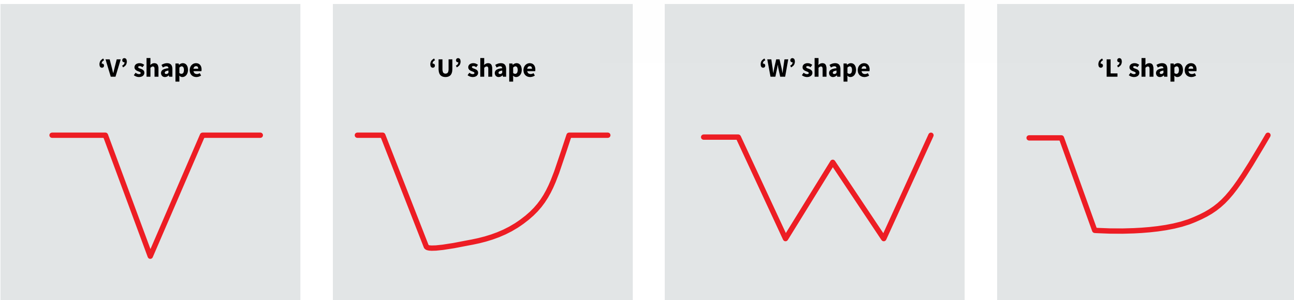
Outlook
The pandemic arrived during a period of faltering global growth, elevated geopolitical risk and an intensifying pushback against globalization. The crisis may exacerbate all those trends. Unlike during the GFC, there is no large-scale international coordination in response as some countries turn inward toward nationalism.

There are three factors which will determine the severity of the economic downturn in each country:
- The extent of the isolation and social distancing measures
- The duration for which they are in place
- The fiscal and monetary policy response

Given the level of uncertainty around the length and duration of distancing measures globally, it is almost impossible for specific-point forecasts to be accurate. Testimony to the uncertainty, Consensus Economics has never seen its contributors' economic forecasts cut so sharply as it experienced in April. Moreover, there is also a significant gap between the most optimistic and most pessimistic; for example, April consensus forecasts for U.S. GDP growth in 2020 varies from -1.3% and -8.5%.

A scenario planning approach
Reflecting the uncertain situation, JLL is looking at different scenarios to see how the downturn and recovery could play out, identifying four example recovery profiles – V, U, W and L shapes.

Economic Recovery Scenarios



Source: JLL, April 2020

The V-shaped recovery is based on a relatively short period of containment measures (circa 1 to 3 months) followed by a sharp return to economic growth with limited second-order effects such as bankruptcy and unemployment. This initially was the base case of many economists; however, as time goes on and the second-round effects become more evident, it seems that we may be moving toward another scenario.

The U, W and L-shaped recovery profiles all envisage some lasting negative impacts that leave economic scars and impact the productive capacity of the economy. They are also likely to show a semi-permanent downward shift in economic activity.

As the exact trajectory of the outbreak and resulting economic effect is unknowable, we suggest a scenario planning approach (as above) with a focus on preparedness and agility.

Global policy response to COVID-19

The COVID-19 pandemic, first and foremost, demands a health policy response. Only an improvement in overall public health will bring an end to the crisis. Although countries around the world have implemented different measures with varying levels of stringency, some patterns have emerged.

Social policy

First, nations have circumscribed social behaviors. Some have restricted the movement of people, both citizens and non-citizens. Governments have restricted travel (both intranational and international) with some placing arriving international passengers into mandatory quarantine, some limiting air travel, and others closing borders. Governments have also shut schools and non-essential businesses, and implemented or encouraged social distancing, with people only allowed to leave home out of absolute necessity. And many countries have banned gatherings, though the maximum size of the group permitted differs from country to country. Increasingly, countries have advised people to wear protective equipment, including facemasks, when out in public.

Health policy

On the health policy front, countries have ramped up testing as quickly as possible in order to understand the full extent of the outbreak. Although some initially lagged in their testing regime, they are now attempting to catch up. Along with testing, nations have attempted to isolate individuals with mild and moderate cases of COVID-19 and provide treatment to those with severe symptoms. Contact tracing can help authorities identify future cases where individuals have had contact with someone with a confirmed positive diagnosis. Countries have also sought to boost the production of health equipment (including masks, faceguards and ventilators), while also expanding hospital and ICU capacity. Some are expediting drug trials and looking for any existing remedies that could prove effective in lessening the severity of COVID-19. Meanwhile, a number of countries are accelerating the research, development and testing of vaccine candidates, looking to shorten the time to successful development and widespread vaccination.

Monetary policy

Several central banks, including the U.S. Federal Reserve and the European Central Bank, have initiated a 'whatever it takes' approach to monetary and banking policy via a portfolio of traditional, recent and novel measures. Despite interest rates already hovering at generally low levels, major central banks have reduced policy rates further, in some cases to levels unseen since the Global Financial Crisis or new record-low levels. Some central banks have initiated or increased asset purchase programs to lower long-term bond yields. In a number of cases, central banks have widened the scope of assets available for purchase, including some (such as corporate bonds) for the first time. The scope of credit programs has also been expanded to alleviate the freezing of credit markets, making funds available to companies including small and medium-sized businesses that possess smaller safety nets. While these measures alone cannot immunize the real economy, they can help to limit the damage.

Fiscal policy

Governments have also utilized strong fiscal policy stimulus to help lessen the impact of the crisis. Initially, many fiscal measures aimed to bolster the healthcare system, but many governments did not stop there, realizing that such actions would likely prove inadequate and require more government spending. In the wake of these measures to support healthcare systems, record-level spending packages across the globe aimed to at least partially fill the void left by the retrenchment in private spending from consumers and businesses. Some measures have targeted ultimate end consumers, while others have been directed at companies in the hope that doing so would help to prevent or lessen job losses. These measures are unlikely to serve as a panacea and we expect governments to expend additional funding once the extent of the downturn becomes clearer.

Real estate policy

Countries around the world have implemented changes to real estate policy in order to lessen the burden on tenants and in some cases landlords:

- In the U.S., many decisions are made at the state and local level, and at least 34 states have temporarily prohibited evictions. At the same time, the federal government issued a 120-day moratorium on evictions from federally subsidized housing or from a property with a federally backed mortgage loan. Major mortgage lenders, including Citigroup and JPMorgan Chase, suspended mortgage payments. Some U.S. states have halted construction on all projects unless essential, such as medical facilities.
- In Europe, several countries, including the U.K., Germany and France, have suspended evictions. A number, like the U.K. and Italy, are providing temporary mortgage relief. In various locations across Europe, commercial and residential tenants have been offered mortgage and rent holidays. Some countries, such as France and Italy, have suspended construction. Banks in Europe are being strongly encouraged to give forbearance and not to foreclose on late payments, while governments have granted retailers tax relief.
- In parts of Asia, some landlords have offered temporary rental rebates and rent discounts. Meanwhile, some countries, like Singapore, are considering legislation that would protect commercial tenants who cannot pay rent for a period of six months.

Policy response summary for 10 largest economies

	Pandemic Response	Fiscal Response	Monetary Response
Brazil	Land borders closed. State of emergency declared through Dec 31, 2020.	R$500 bn (7% of GDP) including unemployment benefits and direct payments to individuals. Direct vouchers for those in informal labor market.	50 bps rate cut. R$637 bn for bank lending. Foreign exchange intervention for liquidity and volatility.
Canada	Closed borders to non-residents. Mutual decision to close US-Canada border to non-essential travel. Only four Canadian airports to stay open for international flights. Schools, museums and cinemas closed with additional containment measures at the province level.	Spending of 3% of GDP, including funding for firms and households, eased eligibility for sick pay, and deferred taxes. Up to 75% wage subsidy for qualifying businesses for up to 3 months to help prevent layoffs.	Policy rate cut to near 0.25%. Purchase of Canadian government securities in secondary market at rate of at least C$5 bn per week.
China	Lockdown of nearly 60 million people across Hubei. Suspended entry of foreigners. Restrictions on movement between Chinese provinces.	Fiscal policy to spur investment of up to 6% of GDP. Funded via CGB (¥2-3 tn) and local government bonds (¥4 tn). 50% interest subsidy to firms impacted by outbreak. Creation of ¥109 bn 'Epidemic Prevention Fund'.	Multiple central bank rate cuts. ¥800 bn refinancing provided to banks to lend to large corporations. ¥350 bn special credit quotas to private and small firms.
France	Closure of all non-essential stores and restaurants. Full lockdown, except for necessities.	€45 bn (1.9% of GDP) funding package, including €8.5 bn for two months of payments to workers. €300 bn of guarantees for bank loans to businesses.	ECB providing €1.2 tn of additional liquidity. €750 bn (6.5% of GDP) 'Pandemic Emergency Purchase Program' bond purchase program. €120 bn asset purchases 'envelope' to be deployed flexibly.
Germany	Borders closed with Austria, Denmark, France, Luxembourg and Switzerland. Banned public gatherings of three or more people. Schools and daycare centers closed. Nationwide closure of non-essential retail activities.	€750 bn, including €156 bn supplementary budget and €600 bn via Economic Stabilization Fund (ESF) - includes €100 bn credit for additional loan guarantees. €156 bn supplementary budget. ESF: €400 bn loan guarantees, €100 bn credit to development bank, €100 bn for direct equity investments in German companies.	ECB providing €1.2 tn of additional liquidity. €750 bn (6.5% of GDP) 'Pandemic Emergency Purchase Program' bond purchase program. €120 bn asset purchases 'envelope' to be deployed flexibly.
India	Travel bans and mandatory quarantines for incoming passengers. All domestic flights stopped. Country-wide lockdown.	US$22.6 bn stimulus package with food aid and direct cash transfers to low-income households. Medical insurance for front-line health workers.	US$4 bn in foreign exchange swaps announced. US$13.5 bn in long-term repo operations at benchmark policy repo rate. Policy rate cuts. US$50 bn liquidity injection.
Italy	Nationwide lockdown.	€25 bn (1.5% of GDP) fiscal stimulus includes: healthcare system and civil protection department (€3.2 bn), employment (€10.3 bn), liquidity for businesses and households (€5.1 bn), local governments (€4.5 bn), tax payments and incentives (€1.6 bn).	ECB providing €1.2 tn of additional liquidity. €750 bn (6.5% of GDP) 'Pandemic Emergency Purchase Program' bond purchase program. €120 bn asset purchases 'envelope' to be deployed flexibly.
Japan	Banned entry of travelers with Chinese passports from Hubei or Zhejiang provinces, and of foreign travelers who have visited certain Chinese regions, South Korea, Iran or Italy within the previous 14 days.	Two aid packages totaling ¥108 tn in total – equivalent to 20% of GDP, including assistance for medical professionals and those affected by school closures, as well as loan support.	Provision of liquidity through commercial paper and corporate bond purchases. Low-cost lending facility set up for corporates impacted by virus. ¥500 bn for bond purchases followed by additional ¥200 bn bond purchase program.
U.K.	Nationwide lockdown. Nationals advised against all international travel for an indefinite period.	Support to businesses via emergency loans (£300 bn), tax cuts and grants (£20 bn). £7 bn emergency spending to support households, businesses, and local governments.	Policy rate cut and expansion of quantitative easing program by £200 bn. Provision of credit to businesses, particularly small and medium-sized firms (approx. £100 bn).
U.S.	No national lockdown but majority of the US population is currently ordered to 'shelter in place' by state mandate. Banning of non-US citizens or residents who have been to China, Iran and some EU countries in the previous 14 days. Borders closed with Canada and Mexico.	US$2.8 tn package (circa 10% of GDP). Supports households, businesses and governments. Includes US$850 bn in loans, US$838 bn in fiscal stabilizers, US$652 bn in tax deferments, US$480 bn in direct spending.	Fed implementation of 'whatever it takes' approach via cutting interest rates to zero, unlimited asset purchases (quantitative easing), and providing liquidity of roughly US$500 bn in total.

Source: JLL Research, 15 April 2020

Are green shoots emerging in China?

Cautious optimism following a relaxation of the lockdown

Are there lessons to be learned from China's recovery profile?
China was the first market majorly impacted by COVID-19, causing unprecedented lockdowns and restrictions on mobility, and resulting in its economy contracting by 6.8% in the first quarter. Two months after the introduction of these measures, the number of new cases in China has declined significantly and the COVID-19 outbreak appears to be stabilizing. However, recent events elsewhere show this unpredictable virus can easily re-emerge. China is now starting to loosen lockdown measures and the world is watching.

At the height of the outbreak, COVID-19 brought most Chinese industries to a standstill. Now, many traditional industries are slowly returning to normal. At the same time, others are seizing emerging growth opportunities with potential positive impacts for real estate markets. These include the digital economy, online entertainment, insurance, healthcare, and real estate technology.

Office sector: The return-to-office rate varies by city, with 80–100% in Shanghai and 75-80% in Chengdu and Chongqing. Leasing volumes have slowed and renewal has become the preferred choice of tenants. The 'new economy' companies appear to be faring relatively well with increased enquiries from tech firms. There is now also an increased focus on safety.

Retail sector: Malls are slowly coming back to life, albeit with precautionary measures including temperature checks and social distancing measures. Leasing activity remains subdued and it is possible that there will be further impacts from the lockdown in Q2. International brands are selectively continuing their expansion plans while grocery stores and supermarkets are benefiting from people staying in rather than dining out. Brands have accelerated their adoption of integrated online and offline sales as consumers prefer to avoid crowded shopping areas.

Logistics sector: The logistics sector exhibited a degree of resilience during the outbreak due to tenants such as e-commerce companies. Freight traffic and warehouse parks have now resumed operations. Trends such as fresh food deliveries have accelerated and demand for cold chain logistics is expected to increase.

Hospitality sector: According to STR, 87% of hotels in China have now reopened, although most are reporting low occupancy rates (below 30%). Restrictions are still in place, with inter-provincial trips discouraged and travel bans on foreign visitors. There are some signs of recovery with improving staycation demand in resorts located an hour away from major cities.

Capital markets: Investors are still showing strong interest in China's commercial real estate market. While the outbreak may have postponed some deals, other negotiations have been pushed through with confidence from investors, particularly domestic. Investors are focusing on the longer-term potential.

For further information please see the full report below:

Re-entry: Operational resilience and the ‘new normal’

Operational resilience will be crucial to recover from the outbreak

Businesses will not go back to the way we knew before the pandemic, but will reinvent themselves to be more resilient, adapting their operational models to the ‘new normal’.

The short-term impact for occupiers is proving to be significant as their business-as-usual activities are affected with changes occurring on a daily basis. The immediate shock and realization of the outbreak is now over and the majority of occupiers are in response mode after a short phase of preparation and immediate actions. Occupiers are preparing for ‘re-entry’ of their facilities and sending their workforces back to work in several waves.

Prepare
Outbreak
Shock & Realization

Respond
Peak
Adaptation & Business Continuity

Re-entry
Almost there
Productivity Challenge & Re-entry

Reimagine
The ‘new normal’
Reimagination, Implementation & Flourish

Source: JLL Research, April 2020

Planning for 're-entry'

There is currently limited visibility on the timing of this next stage but companies are now planning for re-entry. This phase is complex to navigate, requiring some restructuring and courage from business leaders and their workforces. Occupiers must determine the level of modification required to return to business: prepare, redesign and fit-out workplaces ready enough to invite employees back to the office, combined with remote-working capabilities and a robust triage approach. It is not about getting back to the office as soon as possible. Rather the opposite approach. It is first and foremost about technology. What does it take to 're-entry' facilities that were closed weeks ago, bring people back to work and return to a stable business activity? What functions must come back when the 're-entry' option is available?

Corporate re-entry check list

Workforce

'Provide confidence it is safe to come back to work'

- ☑ Eligibility / triage to return to work and identify priorities of re-entry
- ☑ Critical activities and sites identified including site proximity analysis
- ☑ Training and education program to prepare for return to work
- ☑ Social and physical distancing protocols
- ☑ Limit sharing of equipment
- ☑ Provide mental health support

Asset & people protection

'Safety, health and wellness to remain the priority'

- ☑ Full protection through hygiene solutions. Visible and well-trained cleaning staff will be critical
- ☑ Limited / controlled access to manage density
- ☑ Commuting plans and protocols
- ☑ Employee and visitor screening solutions
- ☑ Tracking and control measures using technologies
- ☑ Healthy building measures

Workstyle adaptations

'Changing protocols and workspace design'

- ☑ Reduced workplace density – redesign space to maintain new distancing standards
- ☑ New protocols to reduce gatherings while enabling collaboration
- ☑ Provide new onsite facilities to reduce need to leave
- ☑ Enable remote working to continue

Source: JLL Research, April 2020

Wider environment as important as corporate behavior

Actions by corporate occupiers is only one piece of the re-entry strategy. Landlords along with city and regional / state governments also need to be providing safe environments and clear guidance to employees and corporates alike. Public infrastructure must be adapted to manage density and provide clean environments along with enabling tracking and control measures. Corporate decision-making will depend on the country / state / local policy and measures.

When in doubt, put people first

There is opportunity in adversity in every business. Assistant Professor Joe Allen of Harvard University thinks "we'll soon be in a place where 'acceptable' is no longer acceptable. The goal will be optimal"[1]. Returning to work means reaching an optimal solution where the trust of people in their employer, their colleagues and their government / state is beyond expectations. The physical transformation of our environments is instrumental in reaching this state and crucial to getting back to work. New habits and behaviors will need to be adopted and educated. This 're-set' will lay the groundwork for reimagining the new workplace as a liquid and distributed ecosystem model.

[1] https://www.bisnow.com/houston/news/architecture-design/the-coronavirus-is-going-to-change-how-we-think-about-design-103669?utm_source=CopyShare&utm_medium=Browser

Real estate capital markets

Short-term pullback expected in capital flows as uncertainty builds

Over the short term, investment activity in global commercial real estate is expected to slow. Restrictions and uncertainty around valuation is limiting investors' ability to perform due diligence, and it is more challenging to execute transactions. Delayed launches and elongated transaction timelines are increasingly evident in affected markets as city lockdowns, travel restrictions and social distancing become commonplace around the world. Technology continues to be used to connect parties and reduce some of the barriers to productivity. However, the uncertainty of the duration of the pandemic and the inability to appropriately price risk will maintain higher barriers to the normalization of capital flows in the near term.

On the other hand, the situation in Asia Pacific has provided a benchmark for what a recovery could look like in other regions. In China, life is shifting back to normal for most locations outside of the Hubei province, where the outbreak began. Manufacturing is returning to roughly 90% of full capacity while circa 80% of retail, restaurants and bars are now open. Transactional activity is gradually improving across the region, and investor appetite is growing. However, there is concern in markets such as Singapore, which was initially less affected, where infection case counts have risen due to residents returning from abroad.

Investors look to major arbiters of asset-level risk

Even though sentiment has been dampened, investor appetite in certain segments of the market has remained in spite of challenges to transacting. Healthcare and logistics assets continue to garner interest, especially since many of these have been supported by governments as essential infrastructure and are seen to be defensive and resilient. We expect investors will continue to look to a few considerations as major arbiters of asset-level risk in the near term:

- **Income stability:** The less variable the contractual income, the less risk. This favors the living sectors and office assets with credit tenancies, lower exposure to variable rent and strong remaining terms.
- **Operation criticality:** The more important the facility and tenancy to revenue and business operations, the lower the risk. This favors data centers and critical logistics assets.
- **Occupation density:** The higher the density of occupants, the higher the operational risk of contagion. This creates short-term risk for hotels, retail, select living assets and flex-office operators.

While many investors have paused new acquisitions, select well-funded institutions and high-net-worth investors with longer-term investment horizons will be among the first movers, concentrating on these sectors. Offensive, higher risk profile strategies will emerge in other segments of the market where pricing dislocations may yield opportunities, particularly in the retail and hospitality sectors.

Investors and lenders focused on 'price discovery' and asset management

Despite ample liquidity in debt markets, lenders remain in a phase of 'price discovery' and are increasingly shifting to asset managing their existing portfolios. This is particularly evident in the U.S. where lenders are focused on formulating policies and procedures on how to best manage and underwrite forbearance requests. The stabilization of the cost of debt will be a critical enabling factor in the recovery of transactional activity, and the debt market is expected to be resilient given the stability of the credit markets as compared to the Global Financial Crisis.

In line with direct investment, new fundraising activity is likely to be delayed. Existing mandates in the market, particularly those which were further along in marketing, are continuing to secure commitments and move toward closings. The experience and track record of managers will be of increased importance in investor decisions, and this will benefit established managers throughout and beyond the current market turbulence. The so-called 'denominator effect' may slow deployment of new capital to the asset class in the near term given recent volatility in the public markets. However, it is important to note that the denominator effect is an expected byproduct of a successful diversification strategy, and investors typically have margins around their allocation targets that permit them to overweight or underweight an asset class based on market conditions. In fact, some investors are increasing their target allocations to real estate to be ready to take advantage of anticipated market dislocation. Nevertheless, there continues to be a record level of dry powder (US$330 billion) available.

Over the long term, real estate remains an attractive asset class

Although investment into real estate has fluctuated over the years through various downturns, the overall trend has been for higher allocations to real estate, and we see no reason for this trend to reverse. Real estate continues to offer good risk-adjusted returns that are less correlated to other asset classes. This portfolio diversification advantage of real estate investments is only emphasized in periods of increased volatility in the equities and commodities markets.

Finally, the spread between real estate yields and government bond yields remains at levels that more sufficiently reward the real estate investor. Given this, we expect to see continued flows (and potentially an increase) of capital into real estate over the medium to long term.

A catalyst for change: potential sectoral implications

Although the COVID-19 pandemic is first and foremost a human concern, there are secondary effects that are filtering through the economy and real estate sector that may be with us to stay. The way we are all currently living and working differs vastly from this time last year – those changes which will become part of our 'new normal' following relaxation of the lockdowns remain to be seen. Below, we explore some of these emerging trends by sector.

Office sector

Impact on flexible space demand amid mass remote working

The flexible space sector, which in recent years has accounted for a substantial share of net absorption in global gateway cities, has fallen flat as a direct result of the COVID-19 outbreak. This will likely force significant consolidation across the flex industry.

In the medium to long term, demand for flex space will continue to be an important feature. Many corporates will be anxious not to commit to big capex projects or make any firm employee headcount forecasts, which will strengthen demand for preconfigured space on flexible terms. Furthermore, the forced mass experiment in home-working will reinforce the need for corporates to adopt agile portfolios and adapt the physical office to deliver collaboration.

The trajectory of the office market will be shaped not only by the ability of governments and financial institutions to manage the ongoing crisis, but also the potential emergence of structural changes to how space is used and incorporation of lower employee density and deployment of remote-working options.

While some corporates might look to remote working in order to compress their real estate footprint, most are already looking at ways to future-proof their portfolios. Risk mitigation strategies will include greater investment in 'business continuity planning' space and remote-working facilities. De-densification is also likely as the appeal of highly dense, large, open-plan offices is now clearly up for debate. Finally, social distancing will highlight the value of day-to-day social interactions and our belief that physical interaction is a key catalyst for innovation. While it is too early to make bold predictions in terms of a shift in the quantum of space required by corporates coming out of this crisis, the physical office will take center stage in facilitating interaction and collaboration and, ultimately, employee health, well-being and productivity. It is likely to cater for face-to-face / large group meetings that promote sale connections and collaboration, and not just be a place to come to work every day.

Retail sector

Move toward flexible omni-channel retail models and sustainable fulfilment

For retailers, the primary focus in the short term remains on preserving cash. A rising number of retailers and leisure operators are assessing options to offset the loss of revenue from their physical store portfolios. For example, proactive gym operators are offering subscription services to stream online workout sessions while high-end restaurants are offering meals for delivery or collection, and others have turned eateries into mini supermarkets. Social responsibility is being closely monitored by customers, who are spending more time online as a result of lockdown measures. In addition to generous donations and the manufacture of masks and hand-sanitisers, various cosmetics and luxury brands have embraced live streaming for sharing make-up and fashion tips. The common denominator for retailers is to stay relevant and to be socially responsible as consumers temporarily reign in their spending.

Looking further ahead, many retailers will rethink their operations and supply chains. Having the right infrastructure for the fulfilment of online orders continues to be crucial for trading. As the structural change in the retail market accelerates, greater emphasis will be placed on the shift toward a flexible omni-channel retail model and sustainable fulfilment; strengthened partnerships between landlords and retailers will need to emerge to achieve this. In addition, existing store networks will be reassessed. For example, some upmarket retailers are exploring options to accelerate the opening of outlet stores post-COVID-19 as a means of clearing surplus stock.

Logistics sector

Supply chain risk mitigation and resilience

Supply chain risk mitigation and resilience will become a key focus for operators. Companies will increasingly look at:

- Re-shoring or near sourcing of manufacturing, with greatest pressures on critical industries (such as medical devices, technology and pharmaceuticals). A renewed emphasis on domestic supply chain independence will accelerate this re-shoring trend.
- Greater diversification in terms of sourcing. Distribution networks will be re-set to be less reliant on one country in order to de-risk the production or distribution processes. This will lead to more multi-facility / multi-location strategies.
- Diversification of transport modes, including the development of port diversification strategies and investing in locations that provide multi-modal transport options.

This is likely to result in additional regional demand for manufacturing facilities and associated logistics, but potentially lead to weaker world trade growth and container flows at gateway ports.

Additionally, companies with very lean supply chains (with low inventory cover) may seek to increase their inventory levels.

The pandemic will accelerate trends already in evidence across the sector such as increased online penetration rates, expansion of online grocery, omni-channel retailing and the integration of technology into warehousing. Industrial and logistics fundamentals were very strong prior to the COVID-19 crisis. Occupier demand had been exceptionally robust and vacancy rates were at near-record lows. The pandemic is highlighting the critical importance of supply chains and logistics real estate, and the sector is well placed to respond to the post-COVID-19 recovery.

Hospitality sector

Changing consumer travel preferences

International travel around the world has ground to a complete halt, with many airlines and cruise companies suspending flights and cruises for several months. Once the industry starts to recover, travel patterns are expected to shift toward drive-to-resort destinations and less dense markets where travelers can be in open spaces and avoid large groups of people.

The types of lodging people will gravitate to may also change. The coronavirus' psychological impact on consumer travel behaviors can be compared to the aftermath of the 9/11 terrorist attacks. People have become more self-conscious of being in close proximity to others and are fearful of contracting the disease in public places with questionable standards of cleanliness. Non-professional lodging options, largely comprised of alternative accommodations, are likely to face increasing scrutiny and pressure from guests who are concerned with their health and well-being.

Living sectors

Throughout the COVID-19 pandemic, the living sectors have maintained their reputation for resilence and stable operating cash flows. However, the future peformance of the different living sectors will vary significantly.

Income protection schemes help to support rental incomes in multifamily

Multifamily is widely considered to be the most resilient sector to the real estate impacts from COVID-19, but this will be challenged should growing unemployment begin to soften rental demand. The widespread use of income protection schemes will mitigate against the worst of these impacts provided they remain relatively short in duration. Should commercial activity become more widespread in a timeline similar to China, there is a reasonable expectation that incomes will be supported. The investment risks are weighted toward lower-income rental properties, where workers are disproportionately exposed to structural unemployment impacts. More vulnerable households are more likely to require government income support and, as a result, household financial circumstances will correlate with the strength of national policy measures.

Reduced international student intakes pose a risk to student housing

Student housing has absorbed a range of impacts from COVID-19. With rental income largely pre-paid and protected for Spring terms, many operators have been working to provide forbearance strategies. They will now be adjusting occupancy plans for Autumn / Fall 2020, with the hope that health measures have successfully mitigated the acute risk of students returning to physical class environments. There will be lessons from effective social distancing strategies that have already been in use for students that chose or were forced to remain in student accommodation. At the same time, there may be a material adjustment to the proportion of international students taking up places at Western universities.

This risk to income would place additional pressures on income from domestic students, a higher proportion of whom could choose to live at home during studies. Institutions and student housing operating partners will need to develop effective working partnerships to deliver safe, high-quality education on and around campuses. This will be particularly important as more robust virtual education platforms have been enabled though greater technology adoption during the virus period.

Managing health impacts and mitigating risk in care homes and healthcare facilities

The care home sector has been on the front line of managing the health impacts from COVID-19. Its reputation is facing scrutiny as its residents and workers face a very real threat to life in environments that, by their nature, make it difficult to adhere to social distancing guidelines.

There is wide variation across this sector that caters at one end of the spectrum to generally independent and able-bodied residents in retirement living, and at the other to intensive needs-based care in private hospitals. There are further differences in the underlying level of state support and the obligations on care costs borne by the individual. The result is a very mixed picture of fundamental impacts on the operations of facilities as they respond to COVID-19 challenges. It seems inevitable that the pressures of this unprecedented health event will force further consolidation in the care home sector and it may be exposed to greater regulatory pressures.

Coliving building digital communities

The immediate threat to coliving platforms has become more nuanced at asset level, with buildings that derive more income from corporate workers and longer-term residents proving to be better protected from COVID-19 impacts than platforms that are oriented toward more mobile, short-term residents. One of the main strengths of coliving operators has been the greater reliance on technology to form digital communities, and there is growing evidence of communities' ability to self-help and triage operational challenges in delivering social distancing strategies. The funding structures behind many operators will represent some risk of failure and consolidation, but there does not yet appear to be a diminished appetite from investors to support best-in-class platforms.

Looking beyond the pandemic

The evolution of 'mega trends'

The COVID-19 pandemic will undoubtedly change the way we live and work for the foreseeable future, and new trends will emerge that will become part of our 'new normal'.

But what about the more familiar structural trends which have been shaping the world over the past few decades? JLL has identified and been tracking several so called 'mega trends' impacting the real estate sector for many years – the growth of corporate outsourcing; rising capital allocations to real estate; rapid urbanization and city building; the adoption of new technologies; and the imperative to build a more sustainable future and to take urgent action to combat climate change. Their role in shaping the sector has been undeniable over the past decade but, looking to the new post-pandemic world, what influence will they now exert?

All these trends look set to continue, although with some new characteristics and points of focus:

1. **Growth in corporate outsourcing.** The ongoing health crisis should accelerate the trend of outsourcing over the long term. Occupiers will increasingly seek third-party real estate services to sustain business continuity. There will be increased demand for new workplace design, including more digital, flexible and health-oriented working solutions.

2. **Rising capital allocations to real estate.** The low interest rate environment and financial asset price volatility will support the case for portfolio diversification. 'Flight to safety' in real estate, which continues to offer better relative returns in comparison to other asset classes, looks set to increase.

3. **Urbanization.** The pandemic is unlikely to slow the long-term trend in growing urbanization, but will prompt a rethink in urban design, increasing the imperative to develop truly scalable smart city solutions, to put a much greater focus on public health and safety, and to deliver greater investment in public infrastructure.

4. **Technology.** The mass adoption of remote-working technology through the pandemic phase will likely increase the pace of the Fourth Industrial Revolution, including even more emphasis on robotics, the Internet of Things (IoT), Big Data, and unmanned vehicles.

5. **Sustainability.** There will be an increased spotlight on corporate social responsibility, and through this, greater awareness of the fragility of our society and ecosystem.

Our 'new normal' will take time to evolve. New trends are already starting to take shape as governments, businesses and communities begin to adjust to the post-pandemic environment. But equally, there will be other consequences to the pandemic that will surprise us and that are not yet possible to predict.

Through JLL's unique five-pillar Global Insight Program, covering Cities, Capital, Corporates, Technology and Sustainability, we are closely tracking the impacts of COVID-19 on these 'mega-trends' and we plan to share our insights with you over the coming weeks and months.

To find out how we can support your global real estate market strategy with research insights and strategic advice, please contact one of the members of the global research team.

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JLL's research team delivers intelligence, analysis and insight through market-leading reports and services that illuminate today's commercial real estate dynamics and identify tomorrow's challenges and opportunities. Our more than 500 global research professionals track and analyse economic and property trends and forecast future conditions in over 60 countries, producing unrivalled local and global perspectives. Our research and expertise, fuelled by real-time information and innovative thinking around the world, creates a competitive advantage for our clients and drives successful strategies and optimal real estate decisions.