How COVID-19 is hitting the reset button on the global economy and property

Recessions create stress. Stress on businesses, households and entire industries. As demand for goods and services declines, how these businesses, households and industries react can have a direct impact on property across the globe.

If there was ever a recession that could cause stress, it is the COVID-19 Recession of 2020. Not only is it unlike any downturn we have seen before, but it already has the distinction of being the worst contraction in history. The U.S. collapsed at a 31.7 percent annual rate in the second quarter of 2020 and the economy lost more than 20 million jobs in one month as schools, stores, restaurants, hotels, theaters and other places people congregate were closed. These changes are impacting properties across the globe. Whether they are winners, losers or somewhere in between, major and/or niche property types are sure to provide opportunities for occupiers and investors during this recession and well into the recovery.

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HERE'S HOW WE SEE THINGS:

Winners

INDUSTRIAL / LOGISTICS

DATA CENTERS

LIFE SCIENCES

In-betweeners

OFFICE

MULTIFAMILY

The most challenged

RETAIL

WINNERS

The winners are those sectors that were already benefiting from long-term demographic and structural shifts in the economy, only to see those shifts accelerated by COVID-19. They are also benefiting from the rapid evolution of technology and its application to a specific set of challenges.

Industrial / Logistics

The move to online shopping has been happening for some time now. Internet sales were estimated to account for 16.7 percent of all core retail sales (defined as total sales minus auto, gasoline and restaurants) at the end of 2019. Six months later, that share had surged to 22.5 percent as large segments of the population remained at home to reduce health risks. In the second quarter of 2020, internet sales surged 44.5 percent year-over-year. In this environment, it is no surprise that demand for logistics space is nearly back to pre-crisis levels and occupancy is near all-time highs. When have we ever seen a recession lead to higher demand for space of any kind?

Data Centers

Most of us have been on numerous video conference calls since the national economy went on lockdown. Working from home (WFH) has forced many companies to rely on cloud computing to connect with their employees, and data centers are at the heart of that. Since it's likely that WFH will become a larger part of most corporate occupancy strategies, the demand for data centers is sure to grow even more rapidly in the future.

Life Sciences

If there is one sector expected to thrive in a recession caused by a pandemic, it is the life sciences sector—the industry that is devoted to finding ways to keep people healthy and to prolong life. Already in growth mode due to the aging baby boomer generation, the pandemic is further boosting funding to the sector, leading to higher employment and more need for space.

IN-BETWEENERS

"In-betweeners" are those sectors that are being significantly impacted by the recession, but also have structural factors in place that are creating long-term tailwinds that will ultimately help these sectors re-emerge when the recession is in the rearview mirror.

Office

Major headwinds faced by the office sector are the WFH scenario and the job losses coming out of the recession. In the U.S., office-using industries lost 2.9 million jobs in March and April and are slowly recovering those jobs (+880,000 since April). We estimate it will take about two more years to get all those jobs back, keeping demand for space below pre-downturn levels. In addition, labor force utilization will change, creating a structural dampener on office demand. Put simply, more people will work from home both permanently and on a rotating basis. As a result, as jobs are added, those jobs won't have the same impact on absorption of office space. Demand will rise though as the structure of the economy continues to shift to more service and knowledge-driven industries. This means that as the economy adds jobs, a greater proportion will be in an office-using industry. Netting it all out, there will be a full recovery in office occupancy, but it will be somewhat delayed. For occupiers, these structural shifts add up to a slower recovery and more opportunity. It's important to remember that real estate is intensely local—pricing and opportunities in local markets will depend on both demand and supply in any given market, but the broad national trends suggest that demand growth will lag economic growth.

Multifamily

Job losses will most certainly negatively impact the apartment sector's fundamentals, but there is long-term strength in this sector. Half of the millennial generation is still in their 20s—prime renting ages—and Gen Z is right behind them. By some estimates, Gen Z is even larger than millennials. Finally, as baby boomers retire, many will become empty nesters in need of apartments. We suspect the apartment sector will rebound in fairly short order with many years of strong fundamentals ahead.

THE MOST CHALLENGED

The most challenged sector, retail, had already been undergoing major structural changes leading to reduced demand for space and, at the same time, had been hardest hit by the lockdown.

Retail

With so many stores forced to shut down, retailers have had to move sales strictlyonline. Although people still have to shop and necessity retail (grocery, convenience drug stores, etc.) is doing well, 2020 is expected to see record bankruptcy and owners of retail real estate are facing declining revenues. Restaurants started offering outdoor dining and take out with the hopes of surviving, and others turned their operations into ghost kitchens (see article on pg. 8 "Ghost kitchens: cooking up a response to COVID-19"). After COVID-19, experiential concepts may come storming back. People are pining to go out and shop, eat and be entertained—pent up demand will be unleashed. But there will be longer-lasting implications for certain concepts—the U.S. was over-retailed, so a lot of this retail will need to be reimagined (see article on page 20, "Can the shopping mall survive COVID-19?").

The stresses caused by the 2020 global recession will have a major impact on property fundamentals across the globe over the next several years. The cycle has been deep, and the recovery will be prolonged. Sectors that have healthy demographic and structural drivers will recover more rapidly while others will be more challenged. But for occupiers, it's important to note that the stresses in local markets can and will create opportunities, particularly in the near-term.