THE FUTURE OF OFFICE
- Brandon Huffman, **Rubenstein Partners**

Oliver Senchal: What are the key trends at the moment in the US office market?

Brandon Huffman: The office environment is increasingly being used by companies across all industries as a recruiting tool. The flight to quality and unique product continues to accelerate, which makes it all the more important for landlords to position their portfolios in front of these trends. Commodity offices with basic amenities that simply check the box no longer cut it. Tenants are looking for dynamic environments with amenities that much more closely resemble those of residential buildings, such as rooftop terraces, game rooms, bike share programs, modern fitness centres/wellness centres and community managers. Creating this amenity-rich environment and a sense of place are key differentiators that often more than justify the added cost as tenants are willing to pay up for an office setting that enhances their ability to attract and retain talent.

Another trend that continues is the higher-than-historical ratio of collaborative to private space within a tenant's space. Companies are keen on creating ample collaborative space in the form of open floor plans, small group breakout rooms and amenity space within the suite. The point of well-designed space is to promote this collaboration while allowing for maximum productivity as work can be conducted in a variety of locations within the suite.

OS: We have seen pricing moving higher and higher each year, and it has become harder to find attractive opportunities. Is this a concern for you at present and how are you finding value in the current market?

BH: Pricing has been rising across the board for the last couple of years. That said, you have to bifurcate pricing into two buckets: those assets that look and feel like a fixed income proxy and those that do not. Generally speaking, the assets that have experienced the greatest pricing appreciation by far are these stabilized assets in gateway cities, offices included, that the investor universe is pricing like a bond.

Conversely, what we invest in generally does not look like or resemble a bond in any respect. Our focus is often on vacant buildings, large repositionings or situations with a distressed capital structure. There certainly has been some pricing pressure in what we invest in, but our view is that it is relatively muted compared to the stabilized gateway-type product, particularly in areas where international capital has been ploughing in at record pace. Outside of the gateway cities, a lot of those capital flows fall off. And when you get to the less stabilized product, capital falls off even more. We expect the pricing pendulum to start swinging back in the other direction, and maybe we are even starting to see small signs of that today in certain markets.

OS: What do you think will be the key developments for the industry in the next year or so?

BH: One aspect making its way to the forefront of the office investment discussion is the transportation revolution, with a particular focus on autonomous vehicles. Ultimately, that is going to impact where people want to live, where they want to office, and will have rippling implications across the entire real estate sector. Those conversations are already happening, and with the rapid advancement of that technology, these issues are coming to the forefront of a lot of investment considerations. From our standpoint, it is too early yet to declare winners and losers, but we are starting to more carefully deliberate on the implications of new technologies on our long-term strategy.

From a pricing perspective, there is a lot of dry powder in the system today. I think, in part, it is because everybody is waiting for the other shoe to drop and they may innately think they are going to be able to do better deals in a year or two from now than today. Our experience is that when everybody is thinking that, and when there is so much liquidity in the system, it is not when there tends to be a huge, rapid decrease in pricing. To the contrary, the market usually experiences a severe negative correction in times when people least expect it. So it is not our expectation that there is going to be a huge downturn next year, although we also do not necessarily think things are going to pick up dramatically from the frothy pricing levels today.

OS: Do you think those developments will present significant opportunities for investors in the coming year?

BH: There will likely be opportunities for institutional investors, particularly coming from the technological disruptors. Eventually technology is likely to drive some wholesale changes in our industry. Early identifiers that put in the time and effort to understand the implications and consequences of technology are likely to be rewarded as the future comes into focus.

When you look at the capital flows in particular, most money continues to chase the asset classes that are considered risk off as opposed to risk on. To understand and act on that pricing dislocation is an interesting opportunity as well. We do have office investments in both urban and suburban areas, but it is no secret that we have been largely focused on suburban over the last couple of years and even today, because we think that fundamentals in certain suburban areas actually should support higher pricing. Oftentimes, it is the opposite in some urban areas, where we think the fundamentals actually should result in lower pricing than you see in the market today. I think continuing to take advantage of the capital flows, and where they are or are not going, is something we will focus on, in addition to layering in our bottom-up, alpha-driven approach to identifying and converting a lot of these products from transitional to core over time.