Transportation-Oriented Development and Value Capture Post-COVID

ABBEL

Transportation-Oriented Development and Value Capture Post-COVID

Author(s): Sasha Page

Place:
Washington, DC, United States

Date:
2/2/2021

1015 15th St. NW
Suite 600
Washington, DC 20005

www.rebelgroup.com

How we work and where we do it—especially white-collar work—will be changing, with consequential impacts on commuting, real estate, and value capture. Many forecasters believe that workplace "hybrid" models will be the norm with reduced needs for commercial office space, especially in traditional forms, and maybe more for home offices. This may have a material impact on value capture techniques to fund transportation – which include joint development, tax increment finance, and special assessment districts.

Moynihan Train Hall, New York City[1]

Real estate, transportation, and value capture interdependencies

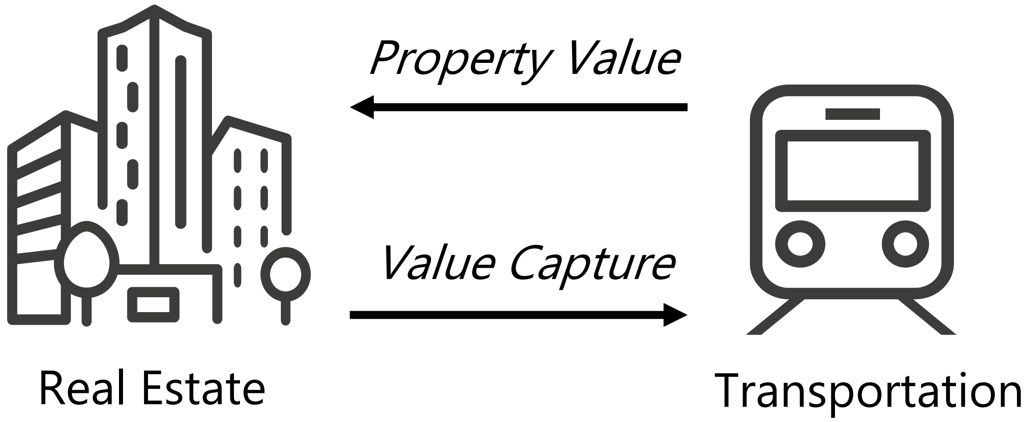
In the past, value capture techniques have been able to fund as much as 20 to 30 percent of major rail and highway projects.[2] Most techniques rely on capturing value from the property at or adjacent to the transit station or highway interchange – doing so through fees, increased taxes, or other ways that value is captured, such as naming rights. This property, or real estate, in

[1] Governor's Press Office, "Governor Cuomo Announces Grand Opening of Moynihan Train Hall in New York City," December 30, 2020, https://www.flickr.com/photos/governorandrewcuomo/albums/72157717626992956

[2] S. Page, W. Bishop, W. Wong, *Guide to Value Capture Financing for Public Transportation Projects*, Transit Cooperative Research Program, Washington, DC, 2016, TCRP RESEARCH REPORT 190, ISBN 978-0-309-45145-1 | DOI 10.17226/23682

turn benefits from nearby transportation services. For instance, the New York Penn Station expansion as shown in the above photo has attracted new office demand. Value capture techniques take a portion of those benefits to fund the original transportation investment and sometimes operations and maintenance. In some cases, this may be a chicken-before-the-egg dynamic since new real estate growth may result in higher value capture monies which, in part, can fund additional transportation infrastructure as shown in the graphic below.

Interdependency Between Real Estate and Transportation



This article focuses on the real estate side of this interdependency and examines how changes in real estate may affect value capture's ability to pay for existing or new transportation infrastructure. Of course changes in transportation infrastructure – like more reliable bus service or stations – also affect real estate values.

The workplace of the future may be hybrid and less traditional

Many workers are working at home, as high as over 40 percent in July 2020[3]. Going forward this may continue. Google, a tech leader known for its innovative office spaces, recently announced it offered to establish a "hybrid" work model in which employees divide their time between home and office.[4] If Google goes through with this, it is likely to influence the

> How we work and where we do it—especially white-collar work—will be changing, with consequential impacts on commuting, real estate, and value capture.

[3] M. Wong, "Stanford research provides a snapshot of a new working-from-home economy," Stanford News, June 29, 2020, https://news.stanford.edu/2020/06/29/snapshot-new-working-home-economy/

[4] J. Elias, "Google will try 'hybrid' work-from-home models, as most employees don't want to come in every day," CNBC, September 23 2020, https://www.cnbc.com/2020/09/23/google-ceo-sundar-pichai-considering-hybrid-work-from-home-models.html

workplace choices of many other tech and office-based firms.

A recent EY/ULI survey found that working from home—or at least not in the office—is likely to be a big theme in the coming years, with 50 percent of respondents reporting that more than 60 percent of employees will be working remotely post-COVID.[5] Furthermore, over half of the surveyed property owners expect to reduce their footprint as a result of changing working patterns.[6]

Most funding leveraged from value capture techniques is driven by real estate values and changes in those values.

A Cushman & Wakefield study reached a similar conclusion—that work from home in the US and Europe will double from 5 to 6 percent of the office population to 10 to 11 percent, while hybrid workers will increase from 32 to 36 percent.[7] Another analyst predicts 25-30 percent of office workers will be "hybrids" by the end of 2021.[8]

The implication of these trends is that demand for office space may significantly decrease overall. Not immediately, but over the next three to five years, as firms' leases come up for renewal. This decline may be mitigated by new health guidelines that may increase space per employee and fewer open plan offices. And with the decline of major downtown and other office locations—everything else being equal—restaurant, retail, and other businesses dependent on the office ecosystem may suffer as well.

Companies will still come together for events, training, and strategy—in traditional and untraditional locations

The EY/ULI study found that more strategic tasks, training, and other work requiring person-to-person contact will remain in offices while day-to-day activities and more routine work will be carried out remotely. In addition, it found that owners expect to see an acceleration of trends that have been occurring for some time: more collaborative and downtime spaces, more space that blends elements of work and hospitality, and more space that is located near other uses, including restaurants, entertainment, and even living spaces—a true mix of uses.[9] Building on the

5 L. van Doorn, V. Raufast, "EY-ULI/Future of Work", https://knowledge.uli.org/-/media/files/research-reports/2020/ey-uli-future-of-work.pdf?rev=0931d121b0e5454988ffe4af72636030, p 11

6 "EY-ULI/Future of Work", p. 6

7 Office real estate market will get back to pre-COVID level, in 2025: Cushman & Wakefield, https://www.cnbc.com/2020/09/27/office-real-estate-back-to-normal-in-2025-cushman-wakefield.html

8 Global Workplace Analytics, "Work-At-Home After Covid-19—Our Forecast," https://globalworkplaceanalytics.com/work-at-home-after-covid-19-our-forecast

9 "EY-ULI/Future of Work", pp. 7-8

tech industry's goal of "making work fun" with "foosball" tables, slides, and snacks—companies will continue to offer amenity-rich offices and environments.[10] New Balance's headquarters, sports entertainment mixed-use development and funding source of a new commuter rail station, known as "Boston Landing," is one of many examples.[11]

And some industry leaders do not think we should "write off" the office just yet. In the Asia-Pacific region, nearly 80 percent of Chinese employers have more than half of their staff back at their desks, according to a CBRE study late last year. And elsewhere, Asian companies say that 22 percent of them will expand their footprint in the coming years, compared to only four percent elsewhere.[12] Finally, a physical space is essential to many organizations' brands for customer marketing. It can also be a critical way to attract talent,[13] so it is unlikely that most firms will go completely virtual—at least in the short term.

> Projects that combine work, play, and living—the office space along the river near single/multi-family housing—may be value capture's "sweet spot."

Projects funded through value capture should anticipate reduced real estate demand

Most funding leveraged from value capture techniques is driven by real estate values and changes in those values. If demand for commercial office space declines, then the value of those buildings may decline, and the dependent tax increment finance district may experience lower and possibly negative growth. Over time, a transit agency may find that choice surplus property next to a station may attract relatively fewer office; hotel; and retail developers interested in long-term ground leases. That is not the immediate case, however, with Facebook's leasing of 730,000 square feet in the Farley Building, which sits atop the expanded Penn Station last year.[14] However, even Facebook may allow as many as half of its employees to work from home permanently.[15]

[10] M. Cooper, "Don't Write Off the Office: Key Takeaways from Industry Leaders in Asia Pacific's Top Markets," Urban Land Institute, December 17, 2020, https://urbanland.uli.org/asia-pacific-edition/dont-write-off-the-office-key-takeaways-from-industry-leaders-in-asia-pacifics-top-markets/

[11] Boston Landing, https://bostonlandingdevelopment.com/map-directions/

[12] M. Cooper, "Don't Write Off the Office: Key Takeaways from Industry Leaders in Asia Pacific's Top Markets,"

[13] Citrix, "The future of office space in a remote work world," November 6, 2020, https://www.citrix.com/fieldwork/flexible-work/future-of-office-space.html

[14] M. Haag "Facebook Bets Big on Future of N.Y.C., and Offices, With New Lease," New York Times, August 3, 2020, https://www.nytimes.com/2020/08/03/nyregion/facebook-nyc-office-farley-building.html

[15] S. Ghaffary "Facebook is the latest major tech company to let people work from home forever," Vox, May 21, 2020, https://www.vox.com/recode/2020/5/21/21266570/facebook-remote-work-from-home-mark-zuckerberg-twitter-covid-19-coronavirus

Rendering of Facebooks' Farley Office Building Offices[16]

Traditional business locations may suffer as candidates for new or expanded transportation infrastructure, if value capture is a material funding source. The special assessment district formed around a traditional downtown may require extra reserves anticipating lower tax revenues or lenders may not accept the location's market uncertainty.

Value capture may be more appropriate for mixed-use and leisure-focused locales

Projects that combine work, play, and living—the office space along the river near single/multi-family housing—may be value capture's "sweet spot." Of course, value capture techniques vary in their applicability by type of project about which my colleagues and I have written[17]. But a high-demand location, like a waterfront, which is less of a commodity and for which tenants may be willing to pay higher rent, should be less susceptible to real estate market fluctuations – a risk that value techniques need to mitigate. The Wharf in Washington, D.C. is one example.[18]

[16] "Facebook's New Office In A 128-Year-Old Farley Post Office Building," United States Architecture News, Oct 7, 2020, https://worldarchitecture.org/architecture-news/efmch/facebook-s-new-office-in-a-128yearold-farley-post-office-building.html

[17] D.'Angelo, T. Edun, P. Hovy, H. Ladley, and S. Page, T. Bishop, S. Natzke, *Value Capture: Capitalizing on the Value Created by Transportation*, Federal Highway Administration, FHWA-HIN-19-004, August 2019.

[18] District Wharf, https://www.wharfdc.com

Value capture techniques should also be used alongside the development of multi-family housing, one of the real estate market's bright spots, where demand is more inelastic.[19] This sector fared relatively well before COVID and likely will afterwards. A segment of homeowners appreciates a more economical footprint in cities and suburbs with walkable benefits, while land use planners appreciate the environmental benefits.

Value capture techniques should also be used alongside the development of multi-family housing, one of the real estate market's bright spots, where demand is more inelastic.

But some housing may have to adapt to new work-at-home requirements, which may include the installation of "phone booth" offices giving at-home workers a quiet and tidy place to video chat, the reworking of the dining room/living room area into a flexible work/relax area, and/or the inclusion of a dedicated home office. Interior designers will be busy!

Focusing on multi-family housing requires addressing affordable housing's deficits throughout the country. If these work-at-home amenities increase housing costs, as expected, this may increase the existing tension between providing affordable housing and maximizing sources to fund transit and other transportation improvements through value capture techniques. Affordable housing's relationship with value capture needs more in-depth discussion.

What can we do to maximize value capture?

Where does this leave transit officials, planners, and other public/private sponsors of major transportation projects considering value capture? While there is uncertainty about when COVID will end and its impact on real estate and value capture, there are several best practices to follow, including:

- **Anticipate how real estate may change transportation needs:** It takes years and even decades to plan and develop new light rail lines or new roads and highways. While we cannot change everything overnight, transportation planners need greater flexibility to change service and, where possible, major infrastructure as real estate and ridership demand fluctuates. High-quality bus service and microtransit shuttles may be more appropriate for certain projects than rail, as they can adapt and more quickly to a decline in demand at one location and an increase at another. As COVID has shown, transportation departments have been able to quickly add "synthetic" bike lanes or change traffic patterns—where there is a will there is a very fast way. This means the

[19] First National Realty Partners, "How Has COVID 19 Affected Multifamily Investments?" November 10th, 2020, https://fnrpusa.com/blog/how-has-covid-19-affected-multifamily-investments/

value capture techniques may be funding smaller assets, such as a flexible BRT line instead of an immovable heavy rail line.

- **Foster mixed-use and fun locations:** Planners and developers should try to focus on projects in locations where employees would stay after work or consider living. Of course, that is easier said than done. And, in theory, the market already does that, valuing the lake view more highly than that of a junkyard. But there are myriad land use and environmental restrictions that make, say redeveloping a waterfront or former warehouse district, more complicated than it should be. These need to be addressed without compromising meaningful planning and resiliency policy.

- **Maximize development flexibility, subject to overarching public policy goals:** Land use planners and zoning boards should give maximum flexibility to developers to choose the use, density, and amenities of a project, within a clearly defined policy envelope. For instance, developers should be allowed to build commercial office buildings that can be easily reconfigured—or parts of them—into multi-family housing units. Zoning should not require ground floor retail but some use that can take advantage of street access and/or foster street life, such as a daycare center or doctor's offices.

- **Build in measures to mitigate funding risk:** Projects that receive funds derived from value capture have always had to address real estate risk. So that application of those risk mitigation measures is prudent today as well, including developing well-devised downside forecasts, utilizing innovative finance credit facilities from the US Department of Transportation's Build America Bureau and some state infrastructure banks (SIBs) that stretch out the repayment loans secured by value capture monies, and relying on value capture techniques that are generally less volatile, like special assessments instead of tax increments.

Value capture as a technique to help fund critical transit, road, and other transportation projects still has lots of "value." But policymakers and developers need to anticipate the possibly significant shifts in the real estate market and work creatively to ensure value capture's continued ability to serve as a critical funding source.

About Rebel

No change without a Rebel

Rebels work on the issues that affect all our futures, from sustainability, transportation and urban development to healthcare and the social sector. We make an impact, not only as consultants but also as investors. After all, anyone who believes in their own advice should be prepared to invest in it. We are committed to bringing change, initiating and realizing our own projects. We provide quality strategic advice & development, business policy & evaluation, partnership consulting & contracts, financial modeling & advice.

Thinking beyond existing structures

The Rebel adventure began in 2002 with ten chairs around a large round table. Sitting around that table, we decided to continue our careers in consultancy by starting our own company – we were the first Rebels. It was to be a company without a hierarchy, without bosses, without limits. A place where everyone could realize their full potential. We bring everything we have inside to the table. Intrinsic motivation, the urge to bring change, expertise and one constant focus: to make a real impact with our projects around the world. We now work with more than 180 Rebels from our offices in Rotterdam, Amsterdam, Antwerp, Düsseldorf, London, Washington D.C., Nairobi, Johannesburg, Mumbai, Manila and Jakarta.

The drive and determination of that first step in 2002 informs how we work with and on behalf of our partners to this day. Trust is everything. In everything we do – and we do a lot! – our objective is to have a positive impact on the world. At the interface between the public and the private, because combining social values with a keen business sense is close to the heart of all Rebels. That might seem like an ambitious goal, perhaps, but we have always relished a challenge. We invite everyone to join in, to become part of the change. Let’s think beyond existing structures. As governments, as companies and as individuals.

Sasha Page
Sasha.Page@RebelGroup

1015 15th St. NW
Suite 600
Washington, DC 20005

www.rebelgroup.com