Global Counsel

Office politics: three perspectives on remote working

28 August 2020 | Author: Gregor Irwin

Summary

Many businesses are feeling their way towards a new balance between remote and office-based working. That partly involves responding to the preferences of customers and staff. It also involves responding to what competitors are doing. The forces of innovation and competition will likely mean the perimeter of the virtual office expands outwards over time. This will have significant implications for productivity; for where economic activity takes place; for globalisation; and for inequality. Many of these changes will be viewed positively by policymakers, but not all. The potential for disruption is highest in areas that are currently wealthier and more economically vibrant. These include some of the largest cities where agglomeration and congestion effects are strongest. Activity will migrate from these economic hotspots to places that are currently less economically vibrant but otherwise attractive for people to live and work. Governments can help or hinder the process through their policy choices. While a move to virtual offices is likely to be net positive, it may face short-term political resistance because it is also disruptive.

Lockdowns have shown that many office-based jobs can be done remotely: some better and some with just a few adjustments. Moreover, they have shown that this alternative way of working is attractive for many businesses, their employees, and their customers.

The mass lockdown experiment has helped to overcome a coordination problem, as many of the benefits from remote working have only became apparent because large numbers made the transition and changed their working practices simultaneously. Now many of the same businesses are grappling with the reverse problem – what should they do now that lockdowns are being eased? Should they encourage their staff back into offices and revert to the old model?

The approaches taken will naturally vary according to the circumstances of each firm and the sector they operate in. The typical approach so far has been cautious, balancing a desire to allow at least some staff back into offices, albeit with constraints on numbers due to social distancing requirements, with a recognition that for many others, working from home remains a better option.

Some firms have gone further. In London, the fund manager Schroders has said it will allow its staff to choose whether they want to continue working from home permanently, even after the pandemic has passed. In California, Facebook says it expects about half its staff to work from home in future. In Munich, Siemens has told its 140,000-strong global workforce, which is spread across 43 countries, that they have the permanent right to work from home for up to three days a week. Others have already fully embraced virtual working, with the web analytics firm Hotjar among those whose operational model is based entirely around it.

Inevitably, a new balance will be found once the pandemic is over. Where that balance is struck remains uncertain. But there are good reasons to believe that this is a moment of structural change, with large permanent changes to how business is done. There are strong commercial motives for that, which go beyond the direct cost savings from remote working. Moreover, the process of innovation and competition may force even the most conservative of businesses to reassess their approach.

This will have implications for economies – both domestic and international – impacting on productivity and growth. That in turn will raise several public policy issues. How those are resolved by policymakers will impact on which changes are likely to be most material and where they will emerge most quickly. All these changes, driven by commercial motives and shaped by public policy, will create opportunities and risks for investors.

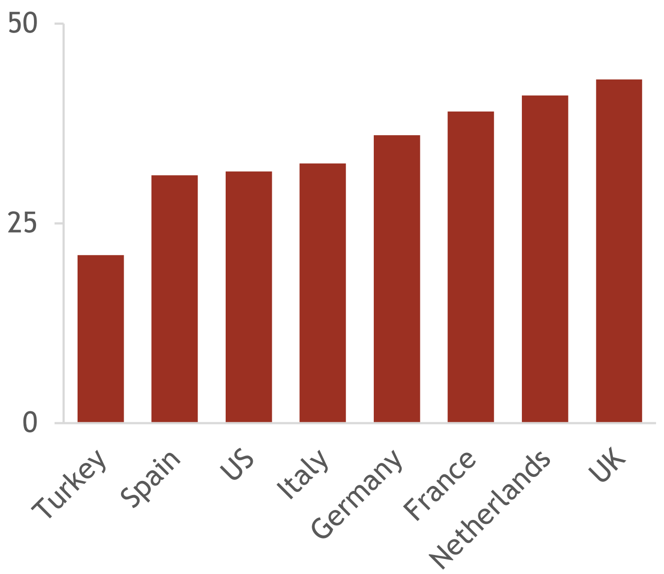
This Global Counsel Insight examines the potential for change to how business is done from these three perspectives – the commercial, public policy, and investor perspectives. Our aim is to identify the issues that each of these groups of decision-makers should be considering now and how the issues interact with each other.

The commercial perspective

Home working is not an option for some businesses. But it is for a large proportion. Fig 1 shows the estimated share of jobs that can be done remotely in certain countries. In the UK, the share is relatively high at 43%, in Germany it is about 36%, while in the US it is 32%. Fig 2 shows separate estimates for the share of jobs that can be done remotely in the US by sector. This varies from near zero in accommodation and food services to more than three-quarters of jobs in finance, management, and professional services.

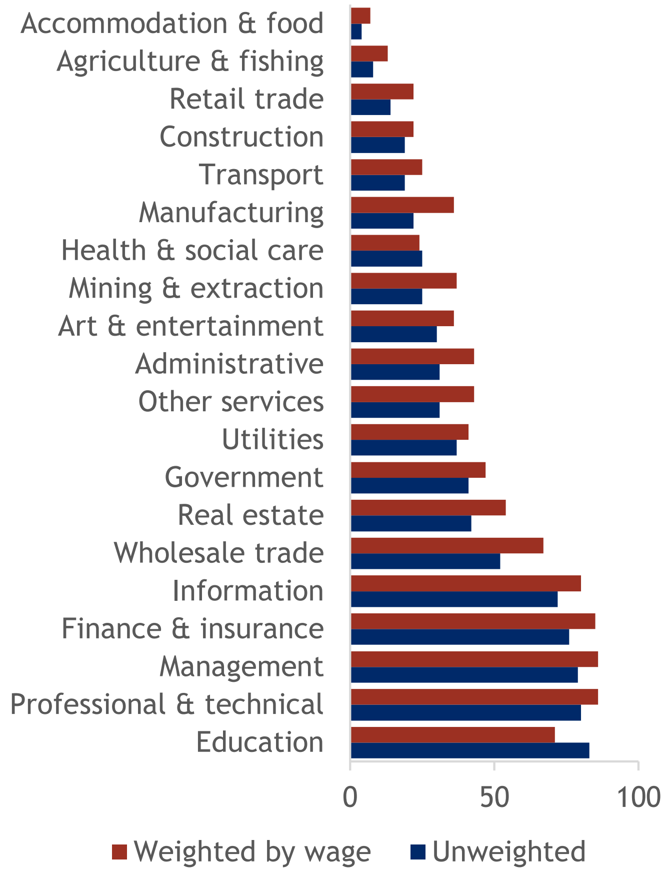
There are some straightforward cost savings that will encourage a permanent shift to remote working. Employees can avoid costly commutes, freeing up time as well as avoiding the need to pay for travel. Employers can reduce spending on offices, including avoiding the additional costs of accommodating employees during the pandemic due to social distancing requirements. However, as Fig 3 illustrates, the potential benefits extend beyond these immediate direct savings, even though some

Fig 1: potential for remote working by country, % of jobs



Source: OECD (2020)

Fig 2: potential for remote working by sector, % of US jobs, unweighted and weighted by wage



Source: Dingel and Neiman (2020)

benefits will only become apparent over time as firms and individuals make further adjustments to how they operate.

One area is recruitment. Employers who are willing to embrace remote working fully will be able to access a wider pool of talent with fewer constraints on where potential staff are located. This will be liberating for firms in locations where the local labour market lacks depth. The flip side is that their employees will also have more reach and can switch jobs more quickly without relocating, for the same reasons. That means a more competitive labour market.

A second impact, which follows in part from the first, is that calculations about where businesses and their employees should physically locate will also change. Employees will have an incentive to move to places that offer a better quality of life and more value for money, when they are no longer tied to being near their employer. Some businesses might not only shrink their physical presence, but also shift it, once the client and employee anchor is loosened, allowing them to choose where they maintain a physical presence based on other criteria, assuming they maintain any physical presence at all.

A third consequence is an accelerated unbundling of services. There has been a steady move in this direction for years, as new technology and online platforms have made it easier for firms to outsource back-office services at a reasonable cost. A shift to virtual working will accelerate this as businesses of all sizes reassess how functions are best performed in an environment where they no longer need to be physically co-located. If, for example, marketing and web design teams do not need to be on the same floor, firms might choose to outsource one or other service.

There is an international dimension to this. If you can provide a service remotely, you can also provide it across borders, unless regulatory or cultural barriers prove to be prohibitive. Regulatory barriers are high in some services sectors, such as financial services. But barriers tend to be smaller for services that are provided by one business to another and are mostly non-existent for services provided within firms. That means there will not only be a dispersion of economic activity within borders, but also across them, as firms shift functions, outsource, or hire staff from locations where the cost-benefit calculation is most favourable.

There are also disadvantages to remote working, with their significance depending on the nature of the business. A shift to virtual offices may allow a greater number and more efficient formal interactions within teams and with clients or customers, once travel costs and the rigmarole of physical meetings are eliminated. But that may come at the expense of the quality of those interactions. This risk is that informal connections between people are weakened, which are important for forging relationships and sparking creativity.

Technology and further changes to how teams work together may help overcome this. Part of

Fig 3: shifting perimeter of the virtual office

Forced office closures → **Flexible home working** → **Full-time remote working**

SHIFTING PERIMETER

Direct benefits:

- Commuting and congestion costs avoided
- Office costs reduced

Full dynamic benefits:

- Labour market reach extended
- Office/home relocation
- Unbundling of services
- Globalisation of services

the challenge is to recreate different styles of conversation between people online. Most firms will also want to consider when and how they choose to bring staff together physically for team meetings or corporate retreats, and when and how they will still want to meet with their clients or customers in person.

There are two areas where the challenges are particularly significant. One is the development of new staff. Only so much can be done through training, either online or in the office. Some development must be done by observing others and by coaching. That is inevitably harder to recreate in a virtual office.

A second issue for regulated industries is compliance. In highly regulated sectors it is harder to enforce controls when you do not have physical oversight of the environment that people are working in.

There is no one model that works for all businesses in all sectors. For now, most are feeling their way towards a new balance between virtual and office-based working. That partly involves responding to the preferences of clients and staff. It also involves responding to what competitors are doing. For some firms, this is likely to be an evolutionary process, while others embrace more radical change. The perimeter of the virtual office in the economy is, however, likely to shift outwards over time as both innovation and competition lead to a new balance being found.

The public policy perspective

The shift towards virtual offices will have macro implications: for productivity; for where economic activity takes place and therefore for economic imbalances; for the international counterpart to this; and for inequality. Many of these changes will be viewed positively by policymakers, but not all. They will also have implications for policy choices in several areas.

The impact on productivity is likely to be net positive and increasingly so over time. Virtual office working widens the set of options for how many firms operate and the fact that many will choose to embrace virtual working reveals that they see net benefits to their productivity.

But there are also benefits - and costs - that will not be internalised by firms and which must also be considered when assessing the net benefits to the economy.

One benefit is the increase in labour market efficiency described above. Some of the gains from that will go to employees rather than firms. The labour market benefits are potentially significant, as we are likely to see an increase in labour supply, as well as greater efficiency. Some people who may not have been able or willing to take jobs requiring physical presence, perhaps for childcare or other reasons, may choose to do so when they can be done virtually. Couples that have needed to prioritise the career of one over the other because of the constraints created by the need to locate in one area may find that constraint is eliminated.

Some other impacts are more mixed. Large cities with concentrated workforces can foster innovation by enabling ideas to permeate through informal social contacts. That may be hard to replicate when people work remotely, implying a productivity cost to be weighed against the benefits. However, it is notable that two of the sectors that benefit most from this effect – the tech sector and financial services – are in the vanguard of change.

The implications for economic geography – where economic activity happens – are also likely to be significant. OECD economists estimate that there are big regional differences in the proportion of jobs that can be done remotely. In the UK, this ranges from about 36% in the north east of England to close to 55% in London. In the US, it ranges from about 26% of jobs in Mississippi to close to half in the District of Columbia. In Germany, it ranges from from below 30% in Chemnitz, in the eastern state of Saxony, to around 45% in Hamburg.

These estimates suggest the potential for disruption is highest in areas that are currently wealthier and more economically vibrant. These include some of the largest cities where agglomeration (and congestion) effects are strongest. A structural shift to remote working will mean that economic activity migrates from these economic hotspots towards places that are currently less economically vibrant but are otherwise attractive places for people to live and work. While this might initially be driven by migration of remote office workers, it will be compounded by the relocation of some businesses and by the indirect impacts of spending locally by migrating workers and businesses. Rural communities are likely to share some of the benefits, assuming they have the required digital infrastructure.

Most policymakers will welcome these changes, but there is a caveat, which is that some jobs may move to other countries. Jobs that can be done remotely, might equally be done across borders, making services the next frontier for globalisation. Greater international trade in services will increase the productivity gains, but also impact on how these changes are viewed politically.

This links to the fourth macro implication of remote working: as well as affecting where economic activity occurs, domestically and internationally, these changes will have distributional effects and therefore impact on inequality.

The beneficiaries are those people whose jobs can be done remotely and whose competitiveness is strengthened by the changes to the labour market, nationally and internationally. These will be the people with skills and expertise that are relatively scarce in a labour market where the reach of many workers and firms is extended. That is likely to reinforce existing inequalities. Fig 2 shows that the jobs that can be done remotely tend to be those that are already better paid. This means that while remote working may lead to a levelling up by place (ie, geographically) it may also widen income differentials between people.

These macro impacts raise several issues for policymakers. At a strategic level, there is the question of whether to embrace change or resist it. The case for embracing change is that it is largely inevitable, on balance positive, and increasingly so over time. The case for resisting change is that it is disruptive and comes at a time when there is already considerable economic uncertainty. Arup estimate that for every 100 office workers in London another 18 are employed in retail, hotels, food and beverages and entertainment. Their jobs face immediate risks. Resisting change may therefore have short-term political appeal.

Policymakers control several levers that can be used to help or hinder remote working, or to mitigate some of the impacts that are undesirable. They can literally help to accommodate remote working through planning controls, for example by making it easier for people to build home offices, for firms to relocate, or for developers to build shared office spaces in new locations. The latter may prove popular as remote working does not necessarily mean home working. Many remote workers may prefer to use shared offices, albeit close to where they choose to live.

In some segments of the labour market a move to more remote working could see more people acting as contractors rather than as employees. This can be helped or hindered by employment law and tax administration. Governments that want to support remote working may want to consider whether the rules in either area create unnecessary barriers.

There is a risk that some governments choose to compete for internationally mobile jobs by offering favourable tax regimes or by weakening labour standards for workers who are not based in offices. That could lead countries to undercut each other, diminishing the tax base and further increasingly inequality.

In highly regulated sectors, there may be genuine concerns among regulators about decisions being taken by people operating outside their jurisdiction, who are not directly subject to control. That could provide a rationale for placing limits on where decision-makers are based. There is, however, a risk of that being abused, with policymakers using such limits as a cover for protectionism where they want to stop jobs migrating overseas for economic or political reasons, rather than because there is a strong regulatory rationale.

In some circumstances, firms may need to ensure that remote working across borders does not violate data transfer rules. For policymakers, there is the related issue of whether existing rules remain adequate as working practices change.

The investor perspective

A point of structural transition in the economy creates opportunities as well as risks for investors. These can be grouped under four headings: real estate; facilitation; ancillary services; and infrastructure. In addition, some businesses will emerge stronger than others in the sectors that are disrupted.

There will be residential real estate opportunities in locations that are economically strengthened by the structural changes. These will tend to be places that are currently cheaper, but where people will want to live once the constraints of commuting are loosened. There will be commercial real estate opportunities as some companies choose to shrink and relocate their physical presence. There will also be opportunities in providing share officed spaces in areas where the residential real estate market is picking up. Companies like We Work that provide shared office spaces have the right model, but possibly the wrong footprint, as this is typically currently concentrated in large city centres.

There are broad opportunities in facilitating home working. One sector that is already benefitting is the tech platforms that make remote working easier, such as Zoom and Slack. There will be more innovation in this area as providers find solutions to some of the practical challenges posed by remote working, such as improving the quality and informality of interactions within teams and with clients. Other forms of facilitation include providing hardware, ranging from technology through to home office equipment. Companies that supply prefabricated garden or home offices are obvious beneficiaries.

Business and remote worker needs for ancillary services will also change, creating new opportunities. People will want gyms and retailers close to where they live, not where their employer is based. The demand for cleaning services will also shift away from offices towards homes. Childcare services will likely see higher demand but need to be more flexible, to match the increased flexibility in office working. Demand for training will change, with more provided online than in the office. But there will also be increased demand for residential training and corporate retreats, as employers seek ways to bring staff together. That means that there will be opportunities for investors in venues that will be in demand and in the providers of these services.

Infrastructure needs will change. High quality broadband infrastructure is essential, not only in urban areas, but in remote rural locations. Transport infrastructure needs will change. Less commuting will alleviate the stress currently placed on some parts of transport systems, reducing the need for investment there. That may free up resources and focus demand in other areas, such as for more user-friendly local transport infrastructures, with smaller-scale and localised public transport and better facilities for pedestrians and cyclists. We are also likely to see a restructuring of some city centres as demand for offices diminishes, creating opportunities for this to be repurposed.

The companies that benefit the most are those that are the most innovative and best able to compete in an environment where changes are occurring rapidly. This will include firms that are best able to strip out costs from their current physical footprint and manage the transition to a new way of working that enhances their appeal both as an employer and to their customers.

Firms with strong brands as employers – those that workers want to be associated with because it boosts their career prospects – will benefit more than others, as this will allow them to extract a bigger share of the net benefits from a more efficient labour market.

A third category of firm that has the potential to benefit is specialist providers of services. They will find new opportunities from the unbundling of services supply chains.

This Global Counsel Insight note was written by Gregor Irwin, Director at Global Counsel.

To contact the author, email:
g.irwin@global-counsel.com

The views expressed in this note can be attributed to the named authors only.

A: 5 Welbeck Street
T: +44 [0] 203 667 6500
E: info@global-counsel.com
www.global-counsel.com
@global_counsel