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URBAN AFFORDABILITY

CHALLENGES AND SOLUTIONS

ILLUSTRATION: JAKE READ

How can cities foster innovation and attract talent when costs and inflation are pushing young businesses to the margins? And how are cities addressing residential affordability and quality of life to draw such talent?

Rising costs are impacting all aspects of life in 2023 and the real estate sector is no exception. It's a troubling scenario for both commercial and residential occupants.

High inflation rates have clear knock-on implications for businesses – smaller firms and startups especially. As their operating costs rise, they are likely to find it harder to afford the commercial spaces they seek in the locations they want, which may limit their ability to grow.

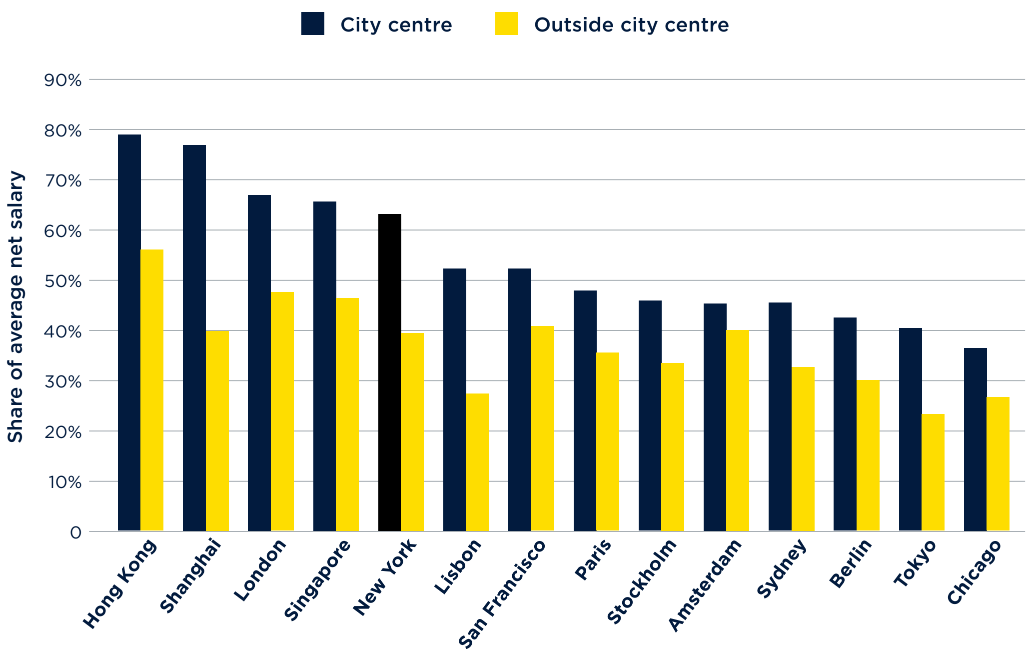
These businesses' most important asset is their workforce, which faces an acute shortage of affordable accommodation local to their workplace. This could pose challenges for recruiting and retaining talent.

At the same time, competition has been rising for high-quality office space over recent years, pushing up rents. Demand continues to increase as businesses of all sizes seek energy-efficient, flexible, imaginatively designed units in well-connected locations that will attract top talent. Covid-19 lockdowns generally reduced completions, setting back construction schedules and causing supply-side material shortages.

Savills Research shows that between 2019 and 2022, prime office rents increased across most major global city centres, despite the disruption caused by the pandemic. Dubai tops the ranking, with rents up 25 per cent, followed by Berlin (23 per cent), downtown New York (17 per cent) and the West End of London (13 per cent).

Small and medium-sized enterprises (SMEs) are again being hit hardest by this upward trend. In many cities, rising rents have rippled outwards from the historical central business districts, pushing up prices in the more affordable fringe areas. SMEs are being forced farther out into more remote districts and less attractive buildings.

ONE-BED RENT AS SHARE OF AVERAGE SALARY



Source: Savills Research using Numbeo

The issue here is partly one of how to protect and nurture small businesses. According to the World Bank, SMEs account for about 90 per cent of businesses and more than 50 per cent of employment worldwide.

Off-the-shelf solutions

Potential solutions are emerging. One is the rise of commercial co-working spaces, which offer all-in packages without restrictive long leases. Given the costs of setting up and maintaining an office, these deals can work out simpler and cheaper over time.

To compare the cost of a co-working arrangement relative to the net effective cost of a conventional prime office, Savills Research assumed a 10-person business, operating across 16 key global markets.

The study found that a co-working space is 40 per cent cheaper on average, although there is considerable variation between locations. While co-working costs 63 per cent less than renting a prime office in Mumbai, the differential is just 14 per cent in Sydney. The cheapest cities for co-working include Mumbai, Madrid, Shanghai, Amsterdam and Los Angeles. New York and London are the most expensive.

Cal Lee, Global Head of Workthere and Savills Flex Co-Head in the UK, notes that for companies starting out, any savings made on premises and channelled into the business could prove the difference between success and failure.

"For any mature office market hoping to have a strong base of start-up and scale-up businesses, it is imperative there is a diverse range of space available from a price perspective. Co-working can be a very affordable route for a young business and it is vital for any start-up ecosystem within a city," Lee says.

Nurturing the start-up ecosystem

Nonetheless, even co-working arrangements may be too expensive for the smallest start-ups. In these cases, public-sector funds are being used alongside private investment in the creation of start-up hubs. These offer cheap rents and share resources among similarly small-scale enterprises in convenient locations.

Beyond affordable rent, co-working arrangements also bring people together to foster collaboration across communities, locally and within their industry sectors.

The Factory Berlin project is a great example of how public and private-sector funding can make such communities viable. Members can choose from a variety of membership plans, ranging from part-time desks to full-time private offices. It means that they only pay for the space they need and can afford, and are not burdened by lengthy leases or high upfront costs.

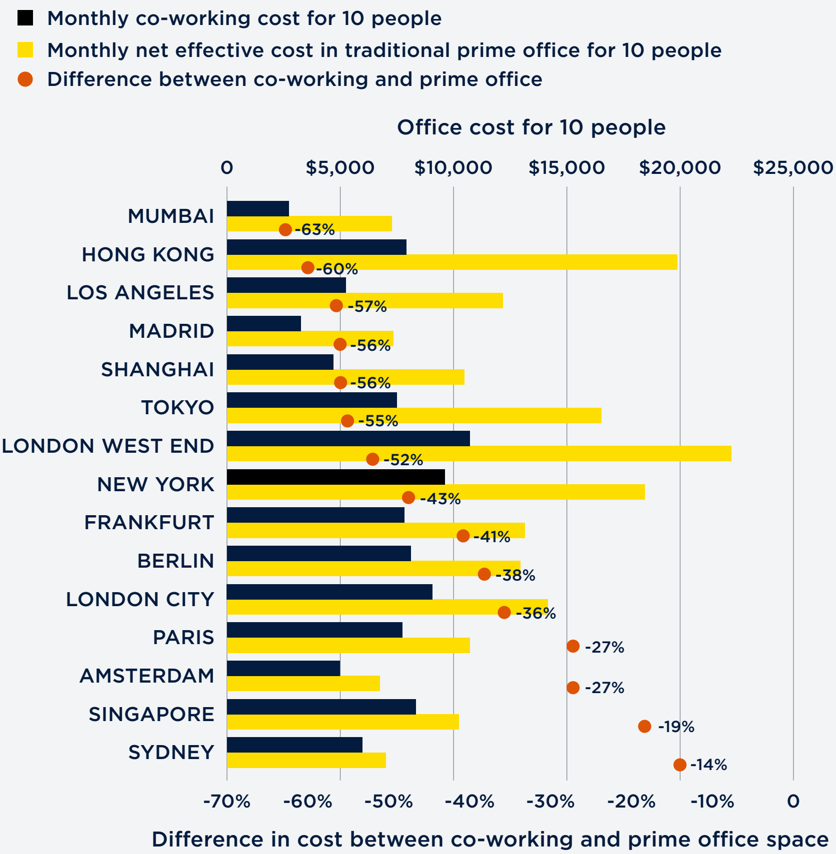
Incubators and accelerators

Similarly, university incubators support enterprises and start-ups driven by the university community, helping to retain academic talent.

Corporate accelerators provide mentorship, resources and funding to early-stage businesses. For the corporates supporting these initiatives, it's a valuable chance to engage with innovative start-ups and the talent they attract.

The 4,400 sq m JLABS @ Shanghai is the first Johnson & Johnson innovation hub to be established in Asia. It can

COST DIFFERENCE BETWEEN TRADITIONAL AND CO-WORKING SPACE



Source: Savills Research and Workthere accommodate more than 50 life-science and healthcare start-ups and larger companies, and provides lab facilities, equipment and mentor support.

Pushed up and priced out

On the residential real estate front, too, affordability pressures are acute. Many city dwellers, especially younger people, students, and essential workers and their families, are affected.

Ageing populations and a rise in single households mean intensifying competition for a limited supply of affordable city housing. Both capital and rental values have been pushed up, with demand for rental accommodation exacerbated by recent hikes in mortgage rates that have thwarted prospective buyers in many big cities.

Historically, an affordable rent would cost less than 40 per cent of net income. These days, tenants in most city centre locations can expect to pay more.

Yet existing social housing stock is failing to keep up with the growing demand for affordable accommodation. New York's City Housing Authority has just 178,000 such units; London has almost 800,000, but supply has shrunk over the past five years; in Hong Kong, you can expect to wait five years for a public rental home.

Frustrated and outpriced, renters are having to look further afield, live at home for longer, move to cheaper cities or "hutch up" by taking a room in a shared flat.

That pressure has refocused attention on the need to deliver genuinely affordable social housing, usually through some form of public-sector support.

As Helen Collins, Head of Affordable Housing Consultancy at Savills, observes: "To increase supply, nations and regions need to put in place clear strategies, targets and delivery models underpinned by state funding, land supply and policy support. Continuity, consistency and certainty provide developers, investors and providers with the confidence to invest."

Such models can take many forms. For instance, in Spain and other EU countries, Covid-19 recovery funds are being used to subsidise affordable housing. The UK provides housing associations with direct grant funding, while in the US investors are incentivised by tax credits to fund affordable accommodation.

Singapore and Hong Kong, meanwhile, run extensive and heavily subsidised public housing schemes for local residents, although they are among the most expensive places in the world for expatriates to buy or rent privately.

Repurposing old commercial stock

Other potential opportunities to boost the availability of affordable stock in city centres include the repurposing of old commercial stock into new housing and the regeneration of deprived neighbourhoods through a mix of affordable and market housing alongside commercial properties.

One example of repurposing in action is Les Grand Voisins – located in Paris's former Saint Vincent de Paul Hospital – which was developed as a temporary but very successful 'meanwhile' mixed-use space for the local community to connect with society and work. For entrepreneurs, rentable workspaces are available.

A relatively recent financial development has been the expansion in the UK and Europe of closed-ended ESG-focused social housing funds from the likes of Man Group and Civitas, among others. These bring private capital to support publicly-funded social housing schemes, with investors accepting a lower financial return than those of full-blown commercially focused funds.

Clearly, there's a pressing need to reimagine city-centre living and working in many big cities, and to make it more affordable in a 21st-century context. The most successful schemes are likely to be those that focus on delivering wider social and environmental benefits, too. ■

GETTY IMAGES

Barcelona: space to innovate

Barcelona policymakers are on a mission to attract talent and make the city a European hub for start-ups.

Barcelona Activa, the local development agency, offers incubation spaces and added services to new start-ups. Three of Barcelona Activa's incubators are located in 22@, the city's innovation district. Small spaces at its four incubators are 30 per cent cheaper than the market rate, while its Technology Park, which is specifically aimed at companies scaling up, offers up to 200 sq m at between 15 per cent and 25 per cent less than in the rest of the area.

"Bringing economic activity in an urban, dense area generates interactions that foster innovation and boost the entrepreneurship ecosystem, says Mario Rubert, Director of City Promotion at Barcelona City Council. "At the same time it produces a transformation toward a better balance between working and living."