THE COWORKING TREND

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Before there was coworking space, the terminology for shared workspaces was often the reliable phrase "serviced offices." In some places around the world, the latter phrasing is still used and often interchangeable with coworking. The big company in the coworking space was Luxembourg-based Regus, now called IWG plc. Then WeWork updated the look, the feel, and the whole concept of shared workspace, thus creating an even newer phrase: "collaborative workspace." The marketplace changed quickly when IWG (then Regus) introduced its Spaces coworking concept. They had to do something, because back in 2016, as one financial writer noted, Regus boasted 160 million square feet of space, but had a market capitalization of $4 billion, while WeWork had just over 5 million square feet of space and a market cap of $16 billion. People liked WeWork's space and its stock.

WeWork blew into the big cities and was competitive immediately. However, depending on where the coworking space was located, the effect, timing, target market, and implementation were considerably different. Three SIOR professionals in London, Toronto, and Dallas confirm the variations of coworking in the respective markets, and the trend lines ahead.

Though Regus has been providing coworking space for almost 30 years, the latest entrant to the market - WeWork - has adopted a different approach to securing market share, says Iain Rackley, SIOR, principal at Avison Young in London. In WeWork's case, this has been through creating coworking communities in large buildings, typically 100,000 square feet to 150,000 square feet. As such, Rackley sees it as capturing the zeitgeist of coworking being a shared activity.

The significance of coworking office providers to the Central London office market can be seen in the office take-up figures. Coworking space was about 20 percent of London's total let-up last year, as compared to 10 years ago when it was just 1 percent to 3 percent. London's main serviced office providers – IWG, WeWork, Workspace, and The Office Group – now provide a wide range of coworking environments, from high-end private club-type space to utilitarian, "trendy" space. This is several iterations on from the serviced-office provider being the main recycler of secondhand space, loaded up with desks and limited regard as to how that space could be used.

To fill all this space, operators have become smarter in the way they market space. First, rather than fill desks with small, start-up companies, co-work operators who are taking large units of space are looking to larger companies to fill their space. So, instead of a start-up company with 10 techies, operators are looking for professional service organizations - lawyers, accountants and others - to sign up 50 to 150 desk positions. This will provide a solid core of revenue that will boost the value of the operator's equity. The "win" for the occupier is trading off a premium opex cost against limited capex (U.K. tenants do not receive much in the way of tenant improvements from building owners) and significantly lower contingent liabilities.

Part of the marketing has been aimed at getting the brokers onside to bring in footloose occupiers through paying broker's fees. Rackley says that in the U.K., the traditional approach has been for the building owner and the occupier to pay their own advisers' fees. In the coworking market, the operator will pay the broker's fee – typically, this is 10 percent of contract value on a 12-month contract. In response to having a large amount of space to fill, operators are now offering one and a half to two times this fee level. In addition, the industry is seeing incentives being paid to brokers to get their clients to view specific buildings. In short, there is clearly a big push to get "buns on seats" in coworking space and to get that revenue up.

Regus has been in Toronto for decades, so it is a misnomer that coworking never existed before WeWork came into the market. Rob Renaud, SIOR, managing principal & senior vice president at Devencore in Toronto, believes that what WeWork offers is just a "fancier version of Regus" by offering traditional serviced-offices with concierges, nice reception areas, cappuccino bars, cool fish tanks and artwork to name a few incentives. Other entrants, such as IQ Office Suites, have come into the market as well.

"The problem," as Renaud recalls, "is that we have a very low vacancy rate (around 2 percent) here in Toronto; coworking companies are looking for space, but so are the other traditional users."

Over 10 million square feet of office space has been built in downtown Toronto in the last 10 years, namely large buildings ranging 800,000 to 2 million square feet. The land is too expensive for a coworking company to build in the downtown core as these operators are small- to mid-range users of space. "I've asked coworking companies to take

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space right off the core," Renaud says, "and they say no because their clients can't walk there."

WeWork in Toronto initially went into a brick and beam-style building. In the past, one would not see Regus doing this. Now, they have created a new business called Spaces, which is similar to WeWork but has included loft-style, creative design. WeWork is now going into more traditional office buildings as the options for the "cool" locations are harder to come by.

There is also another new trend coming up. If a big company temporarily needs 10,000 square feet of space for 120 people in a special team, or if a company launches a short-term project, why not lease the extra space? Using co-work space is another way of not taking on as much risk. This is what some corporations are doing, Renaud shares. Instead of having all of the space under long-term leases only to find that they guessed wrong, why not keep 10 to 20 percent in flexible space and the rest in permanent space? "This is what we are seeing in Toronto and elsewhere around the world," says Renaud, "especially with the new accounting rules."

The creation and leasing of co-work space started growing in Dallas around 2014. Grant Pruitt, SIOR, president and managing director at Whitebox Real Estate LLC in Dallas, says Dallas was already a huge market for executive suites, so it lent itself well to coworking. "We now have several different coworking firms operating here," Pruitt says, "including Spaces by Regus, Industrious, and Common Desk. WeWork took 70,000 square feet in a 50-story building downtown, more space in a new mid-rise building in uptown, and in a two-story, warehouse-type structure." WeWork has taken space in six locations around the metroplex, but Pruitt has seen coworking operations take space in just about every office class.

Pruitt sees it as another arrow in his quiver to use with clients because, as he puts it, "I'm only on the tenant side."

"I have a client that looks for buildings with some sort of flexible space because it has lots of seasonal workers," he says. "My client can lease space and pay for offices they are not going to use nine months out of the year, or they can go to a building with flexible co-work or executive suite space, lease the space they require 12 months out of the year on a direct basis, and flex in and out of the coworking space in the building for the three months needed for seasonal workers." When leased from a co-work provider, the seasonal workers still have a sense of community. They can use the break room as well as the conference rooms (in the direct space), but the company does not have to pay rent for the nine months the extra space is not used.

The downside for a lot of companies past a certain size is that the cost is so much greater for co-work space. "You are paying double the rent," notes Pruitt. "If you are in a $40 per square foot building, it is going to be $80 per square foot in WeWork or other co-work space. You are paying for the finish, free beer, and flexibility."

The latest trend is the outsourcing of co-work development. A company can lease space and bring in a coworking service provider to create co-work type space. Pruitt saw this happen in Plano, just outside of Dallas. "Say you lease 10,000 square feet in an office tower; a co-work company will build the space out like a WeWork," he says. "It will look like WeWork space but you lease the space on a direct basis, so you have control of the lease. You're not under a WeWork lease. The sales pitch is they are building so much of this, they will be able to build the space so it looks like WeWork at a much cheaper price than the competition."

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