Colliers INTERNATIONAL

OCCUPIER SERVICES

U.S. Flexible Workspace and Coworking: Established, Expanding and Evolving

INTRODUCTION

Office leasing and tenancy dynamics are changing apace. Though coworking and flexible workspace still represents a relatively modest share of overall office occupancy, its footprint is rising and expanding rapidly. The impacts are being felt far beyond the walls of WeWork and Regus. Not only are there more providers—and more types of players—entering the arena, but flexible workspace features, such as shorter lease terms and greater service offerings, are being adopted even in more traditional landlord/tenant leasing.

Coworking is now widely understood and established in the commercial real estate industry, and has become an integral space option for most businesses, be they large or small.

Though existing in several different forms, flexible workspace typically brings together workers from different organizations into one general space, through either memberships or more traditional leases. The original model was to attract freelancers, entrepreneurs, startups and remote workers into a shared setting. Providers normally offer more services than in a typical office lease, including 24/7 access, security, coffee, networking events and even amenities such as gyms and discounts to local restaurants and retail.

However, as the concept matures, the focus is shifting from individuals to larger firms and enterprise clients. The tightening and highly competitive labor market, the rise in gig and remote workers, and the belief that a flexible workspace environment boosts both creativity and productivity is increasingly appealing to corporate America. Corporations are also finding coworking to be a cost-effective and flexible way to expand and contract their space as needed.

The purpose of this paper is to help office occupiers and investors alike to better understand:

- The rationale behind using flexible workspace
- Examples of leasing models
- Types of experience models
- The volume and characteristics of flexible workspace in leading U.S. markets
- Key issues facing the sector

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Key Highlights:

- **Fast Growth** - Flexible workspace continues to grow at a rapid pace, now accounting for one-third of office leasing in the last **18 months alone.**
- **Focus on Enterprise** - Flexible workspace providers are shifting their focus to target larger corporations and enterprise clients.
- **Talent Forward** - Companies are turning to flexible workspace to provide the work environment to attract and retain the best young talent in the market.
- **Diversified Uses** - Firms are leasing shared space for everything from surge space to touchdown space for traveling executives to incubators for new products and project teams, among others.
- **Rare Bright Spot** - Flexible workspace is **one of the few growing sources of office demand,** although it still makes up only a **fraction of the office market, with 1.6% of all inventory** in leading office markets.
- **Changing the Model** - Flexible workspace is impacting traditional leasing models and firms' occupational portfolios, together with the nature of how office space is designed and utilized. Traditional owners are responding with their own flexible space and lease options.
- **Tech and High Wage Markets** - The concentration of coworking space is **almost twice as great in tech markets** as in other markets. Coworking also concentrates in **high-wage markets** and cities with a large concentration of professional services firms.
- **Recession Proof?** – Since the vast majority of flexible workspace came online after the Great Recession (late 2007 to mid-2009), **its performance during a downturn is untested,** but it could provide a buffer to landlords as tenants seek short-term, flexible space.
- **Testing the Economics**- While the growth of major providers, in terms of leasing volume and locations, is undeniable, some providers are highly leveraged and could be susceptible to a market downturn, **particularly if office rents start to decline.**

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FLEXIBLE WORKSPACE BY THE NUMBERS

Flexible Workspace—also known as coworking—has matured quickly and spread widely following the Great Recession. The number of coworking spaces in the U.S.—the birthplace of the movement—has soared from less than 300 in 2010 to more than 4,000 at the end of 2017, for a compound annual growth rate of almost 50%. Growth outside the U.S. has been even faster, climbing from less than 200 to more than 10,000 during the same time period, for an annual growth rate exceeding 80%.

Growth continues to be strong globally, though the pace has been slowing as the market matures. Last year the number of coworking spaces rose 16% in the U.S. and 36% outside the U.S. Looking forward, annual growth in the number of coworking spaces is forecasted at 6% in the U.S. and 13% elsewhere between 2018 and 2022.[1]

[1] http://www.smallbizlabs.com/2018/01/us-coworking-forecast-2018-to-2022.html

FLEXIBLE WORKSPACE MARKET OVERVIEW

For all the attention given to this portion of the office sector, flexible workspace still makes up only a miniscule part of the office market. In 19 major U.S. markets surveyed by Colliers, flexible workspace occupied 27.2 million square feet of office space as of mid-2018, making up only 1.6% of all office space. Moreover, the share undoubtedly is even less in the secondary markets (which were not surveyed as coworking tends to be concentrated in larger metros).

TABLE 1: FLEXIBLE WORKSPACE SHARE OF TOTAL OFFICE INVENTORY

	Flexible Workspace Share of Total Office Inventory 2016	Flexible Workspace Share of Total Office Inventory Q2 2018	Flexible Workspace Share of Inventory Growth 2016-Q2 2018
Manhattan	1.4%	2.1%	52.9%
Other Top 10 Markets	0.9%	1.4%	28.3%
Secondary Markets	1.1%	1.5%	17.2%
Total, All Metros	**1.1%**	**1.6%**	**31.3%**

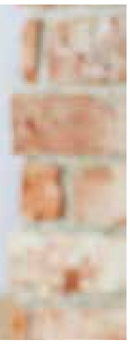
Source: Colliers International Survey

During its August 2018 earnings call, Boston Properties CEO Owen Thomas named WeWork as a key customer. Still, WeWork accounts for less than 1% of the REIT's income.

Nonetheless, the flexible workspace footprint is growing rapidly. Both the amount of coworking space leased and its share of total office space rose by almost half in only 18 months from the end of 2016 through mid-2018, according to our survey.

Moreover, its share of recent leasing has been far greater, equivalent to almost one-third of the office inventory added over the past 18 months. The share in Manhattan is even higher, with flexible workspace equal to more than half of the new supply added. In addition, coworking firms accounted for almost 10% of space leased in Manhattan in the first half of 2018. Indeed, flexible workspace has been one of the few bright spots in the office sector over the past two years, along with the tech sector. Despite a relatively strong economy, job growth is not translating into increased occupancy, making the flexible workspace footprint seem all the larger.

WHERE IS FLEXIBLE WORKSPACE LOCATED?



Our survey identified more than 27 million square feet of flexible workspace. Note that this includes executive suites popularized by Regus as well as the type of space pioneered by WeWork. Almost 40% of that space is located in Manhattan alone, accounting for more than 10.5 million square feet. New York has by far the greatest amount of flexible workspace and also accounts for a higher share of office space (2.1%) than the average of the other large cities we surveyed (1.4%).

TABLE 2: LOCATION OF FLEXIBLE WORKSPACE IN THE U.S.

	Flexible Workspace Inventory 2016	Flexible Workspace Inventory Q2 2018	Flexible Workspace Inventory % Chg 2016-2018
Manhattan	7,144,000	10,506,000	47.1%
Other Top 10 Markets	8,437,000	12,732,000	48.2%
Secondary Markets	2,822,000	3,951,000	47.1%
Total, All Metros	**18,403,000**	**27,189,000**	**47.7%**

Source: Colliers International Survey

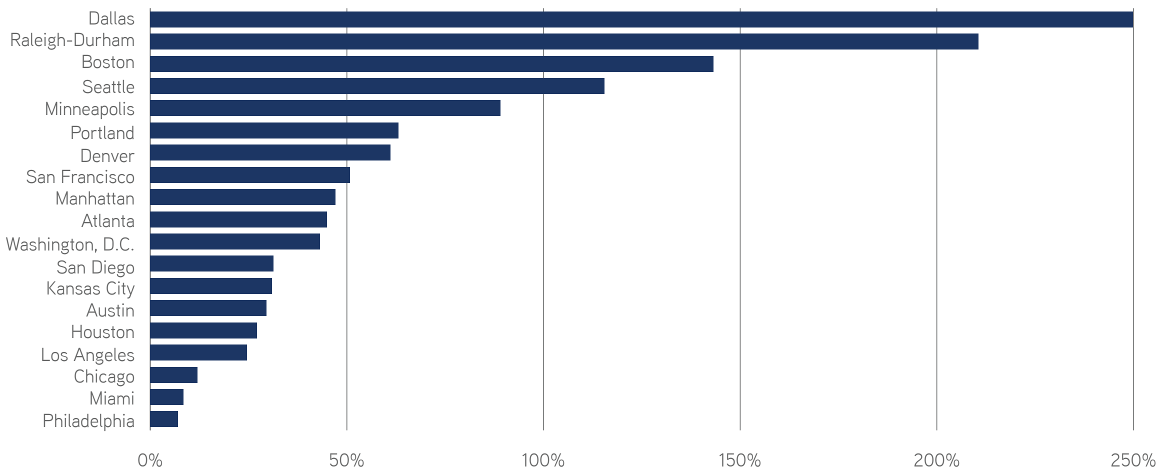
Another 12.7 million square feet of flexible workspace is spread among other major cities in the Colliers 10 leading office markets. While these locations account for a significant volume of flexible workspace, the percentage share of combined office inventory is a low 1.4%.

Finally, we identified another four million square feet of flexible workspace in nine leading secondary markets we surveyed, in which this space accounts for 1.5% of all office space. Perhaps surprisingly, the recent growth rates for both the largest and smaller markets were virtually identical, with each growing by just under 50% in the 18 months covered by our survey. As tech firms look beyond the major cities to attractive second-tier markets such as Austin, Portland and Raleigh-Durham, coworking providers are not surprisingly expanding in those locations.

In terms of individual cities, Manhattan has seen the absolute greatest amount of space added, with more than 3.3 million square feet of coworking leases added since 2016—3.5 times more than the metro with the next biggest inventory growth, Boston, which added just under one million square feet. Seattle and San Francisco also added significant volumes of flexible workspace.

GRAPH 1: FLEXIBLE WORKSPACE GROWTH 2016-Q2 2018

PERCENT GROWTH



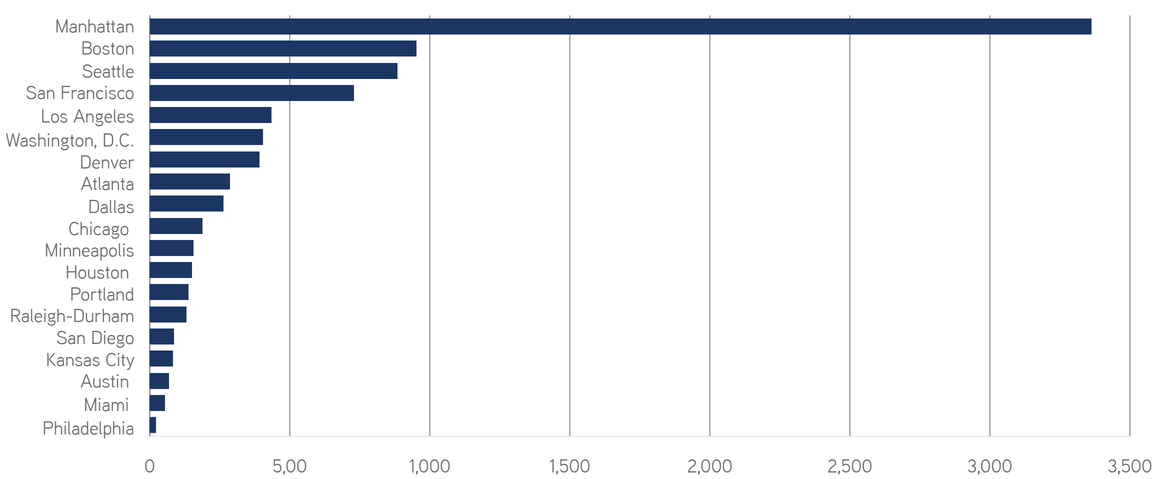
Source: Colliers International Survey

On a relative basis however, coworking has been growing fastest in Dallas and in Raleigh-Durham, both of which saw their flexible workspace more than double in only 18 months. Flexible workspace also doubled in both Boston and Seattle. On the other hand, growth has been much slower and more limited in Philadelphia and Miami.

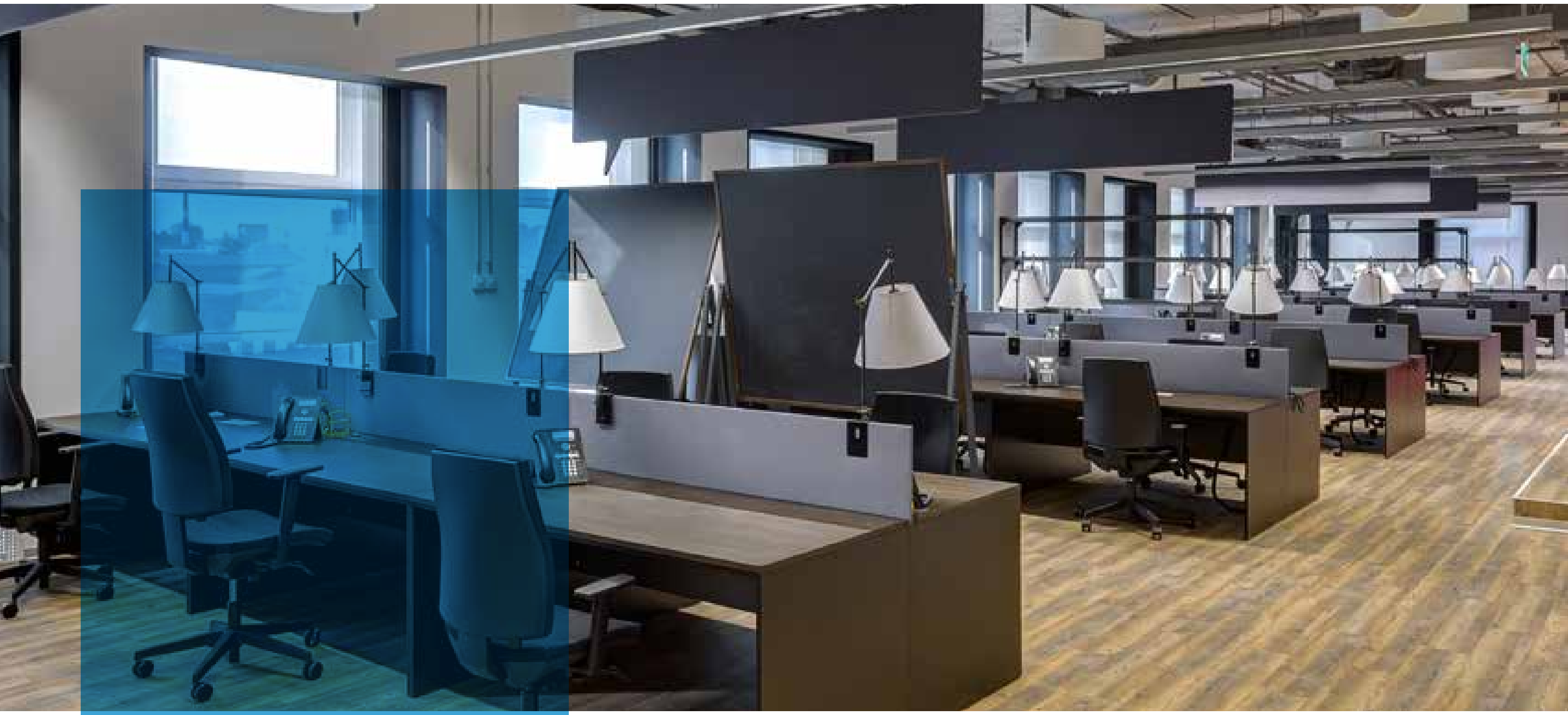
Sensitivity to price differentials also influences the growth of flexible workspace from market to market. In less expensive markets, the price differential between establishing and fitting out one's own space as opposed to using a coworking provider is negligible. The overall magnitude of the obligation is also understandably less. Less obligation equates to less overall risk which may lead start-up enterprises to eschew flexible workspace and its lack of identity.

GRAPH 2: FLEXIBLE WORKSPACE GROWTH 2016-Q2 2018

INVENTORY GROWTH (1,000 SF)



Source: Colliers International Survey



WHAT SECTORS USE FLEXIBLE WORKSPACE?

Tenants from almost all sectors use flexible workspace, but its use is dominated by technology and professional services firms. In markets with a high proportion of tech firms (more than 3% of all jobs in their market), flexible workspace accounts for 2% of all office inventory, compared to just 1.1% in all other markets.

Similarly, there is a strong concentration of flexible workspace in markets with significant employment in professional services and in high-wage markets.

TABLE 3: FLEXIBLE WORKSPACE SHARE OF TOTAL OFFICE INVENTORY

	Q2 2018
Total, All Metros	1.6%
Tech Markets*	2.0%
Professional Servcies Markets**	1.8%
Other Markets	1.1%
High Wage Markets***	1.9%

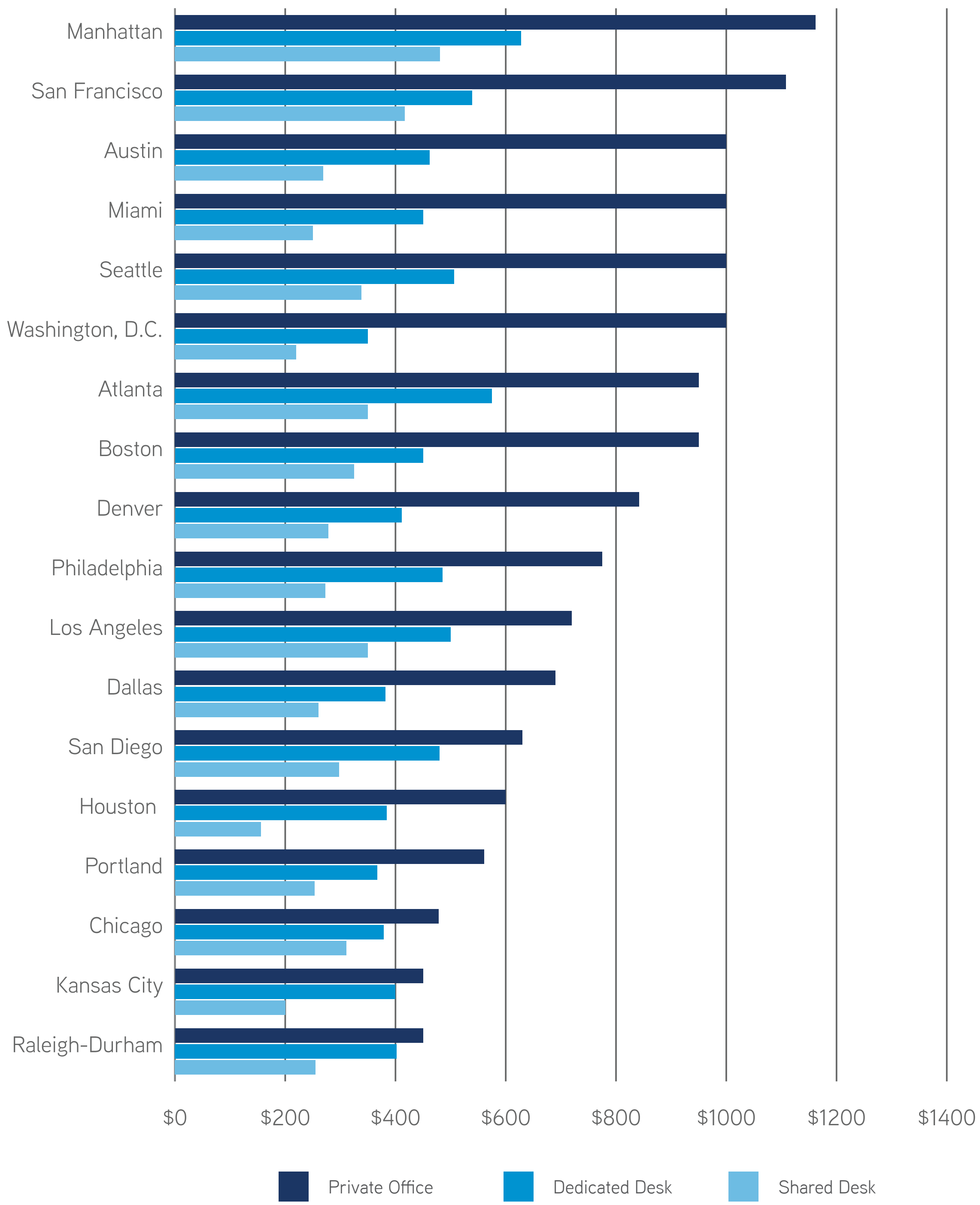
* Tech market = 3%+ of jobs in information services
** Professional services market = 8%+ of jobs in professional or business services
*** High Wage Market = Average income from employment 20%+ Above U.S. average

Source: Colliers International Survey

WHAT'S THE COST OF FLEXIBLE WORKSPACE?

Fees for flexible workspace vary considerably by market. Much of the variation can be explained by the costs of the underlying rent. No surprise then that the average fees per desk are highest in Manhattan and San Francisco, two of the most expensive office markets in the country. Fees are also high in other expensive rental markets like Boston and Los Angeles.

GRAPH 3: AVERAGE SPACE COSTS ($/MONTH)



Source: Colliers International Survey

How do fees for flexible workspace compare to conventional office rents? The monthly cost of leasing a single office from a coworking provider, across the 19 markets surveyed, ranges from $480 per square foot per month in Chicago to $1,160 per square foot per month in Manhattan, equivalent to a high to low ratio of 2.4:1. The spread in Class A rents is significantly wider, ranging from $17.80 per square foot per month in Minneapolis to $97.10 per square foot per month in San Francisco, with a high to low ratio of 5.5:1.

Table 4 compares the annual occupancy cost for 60 square feet of flexible workspace (the typical worker/floorspace provision in coworking facilities) between Class A office rents and flexible workspace fees. The cities are banded in high (more than $50 per square foot), mid ($35 to $50 per square foot) and low (below $35 per square foot) rent categories. The average ratio of annual flexible workspace fee to conventional office rents is 3.2:1. It is lowest in high-rent cities at 3:1 and greatest in low-rent cities at 5.8:1.

TABLE 4: COMPARISON COST OF A SINGLE-SEAT FLEXIBLE WORKSPACE OFFICE AND EQUIVALENT CONVENTIONAL OFFICE SPACE

	Class A Rent/SF NNN	Equivalent Coworking Space @ 60 SF	Average Single-Seat Office Coworking Fee	Ratio
High Rent Cities	$76.07	$4,564	$13,645	3.0
Medium Rent Cities	$43.82	$2,629	$8,867	3.4
Low Rent Cities	$27.07	$1,624	$9,466	5.8
All Cities	**$57.93**	**$3,476**	**$11,237**	**3.2**

Source: Colliers International Survey

Floorspace allocated per worker in traditional office space typically ranges from 150 to 200 square feet, which is 2.5-3 times the 60 square feet per worker in coworking facilities. On the surface, the basic occupancy costs appear to be slightly higher, or similar, for flexible workspace versus regular office space.

However, as companies strive toward space efficiency, flexible workspace offers an immediate savings as opposed to the time and cost of reconfiguring existing office space or moving to a more efficient premises.

The significantly higher ratio in low-rent cities infers only limited price sensitivity to coworking fees in such cities, with tenants willing to pay more for the flexibility and facilities that coworking offers. In secondary cities firms may be testing a new location before considering a longer occupancy commitment. Flexible workspace provides the ability to initially take a small amount of space with a shorter lease term.

Additional factors will impact the consideration between the cost of traditional space and flexible workspace. Space standards vary by market and business sector, while amenity expectations may be greater in high-rent cities. Leasing traditional office space, whether existing or speculative, requires up front time and capital investment that coworking does not. However, flexible workspace occupancy, beyond the short-term, can result in greater recurring costs.

Considerations beyond costs also factor in to tenant's occupancy choices. For example, traditional offices can offer greater ability to retain corporate identity and culture versus the more impersonal nature of flexible workspace.

THE MAJOR PLAYERS

A recent report by Coworking Resources, an independent guide for coworking space owners, listed the largest flexible workspace providers.

- **IWG/Regus:** with approximately 3,000 spaces, is the largest shared-space provider worldwide. Its signature brand of executive suites has 224 locations in our 19 surveyed markets, in addition to 29 of its "Space by Regus" coworking spaces.
- **WeWork:** 341 locations in 65 cities around the world, including 50 in New York City alone, with 200,000 members worldwide.
- **Impact Hub:** 92 locations, with 14 in the U.S., 16,000 members in 81 cities worldwide. Operates as a franchise.
- **Knotel:** offers more than one million square feet of flexible workspace in 45 locations.

Colliers conducted its own study of flexible workspace trends in 19 leading U.S. office markets, and our findings largely track with the global survey by Coworking Resources. Excluding some single-site operators, our market survey identified more than 140 different coworking operators active in the 19 markets, with a total of 27.2 million square feet of flexible workspace in nearly 850 facilities. However, the industry is highly concentrated. The top 10 operators account for 80% of the space; WeWork alone accounts for more than 45%.

The bigger players also tend to have larger facilities. The average space per facility is 39,000 square feet for the top 10 operators compared to just 17,000 for the other 130. Again, WeWork is the leader, with an average size of 79,000 square feet per facility, followed by Level Office with 65,000. Every other operator has an average of less than 40,000 square feet per facility.

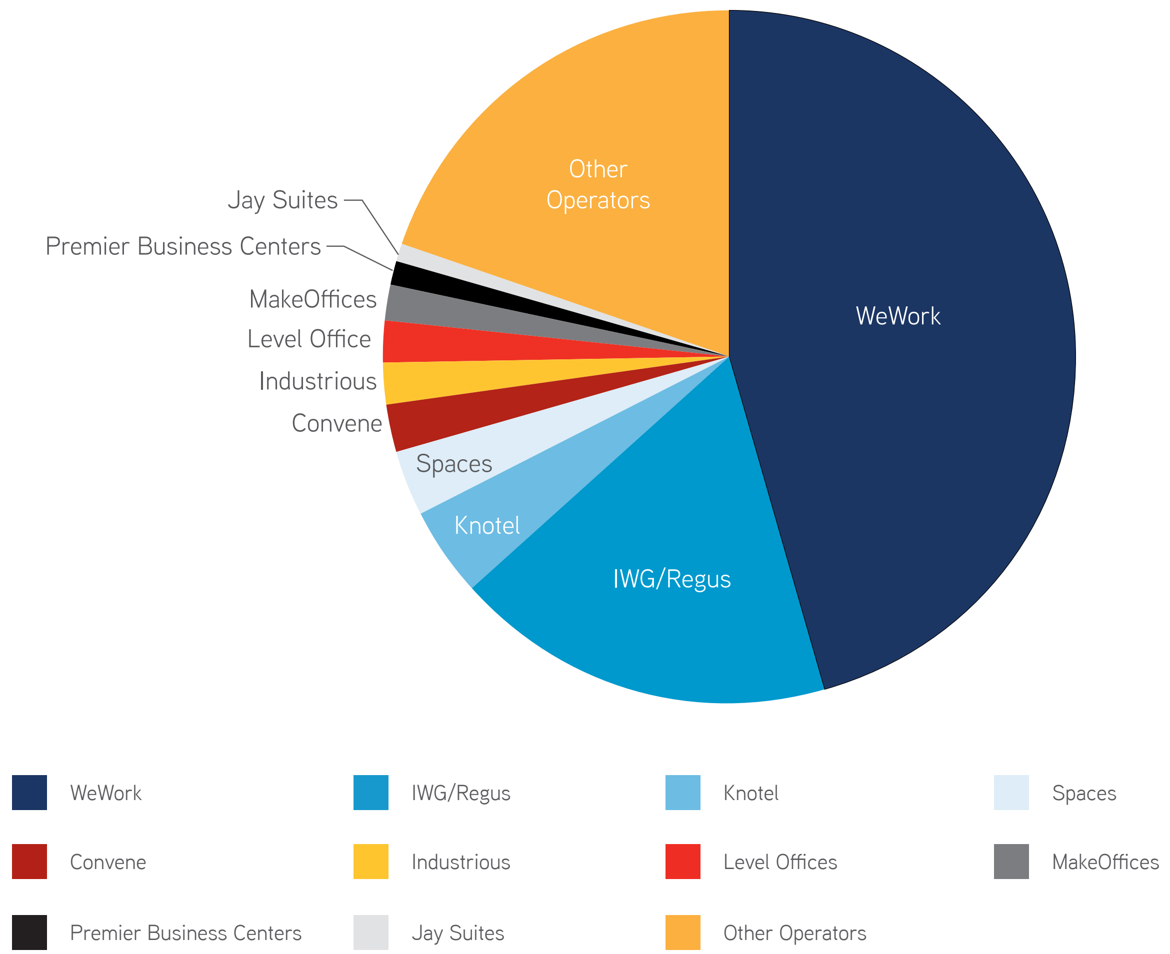
The company with the most sites is IWG/Regus. All told, these Regus sites account for 30% of the sites in our survey, though only 21% of the space, reflecting their smaller average size.

TABLE 5: U.S. FLEXIBLE WORKSPACE OPERATORS

	Total SF Leased	Number of Sites	Space per Site
WeWork	12,162,000	154	79,000
Regus	4,705,000	224	21,000
Knotel	1,127,000	55	20,000
Spaces	835,000	29	29,000
Convene	538,000	14	38,000
Industrious	525,000	22	24,000
Level Office	513,000	8	64,000
MakeOffices	428,000	12	36,000
Premier Business Centers	291,000	19	15,000
Jay Suites	260,000	8	33,000
Top 10	21,383,000	545	39,000
Other Operators	5,806,000	301	17,000
Grand Total	27,189,000	846	31,000

CHART 1: MAJOR FLEXIBLE WORKSPACE OPERATORS

TOTAL SPACE LEASED (SF)



MOTIVATIONS FOR USING FLEXIBLE WORKSPACE

Firms are increasingly adopting flexible workspace—or expanding their use of such space—for diverse reasons, both quantitative and qualitative. From tactical and operational to creative and strategic, large corporations are embracing the flexibility that coworking offers, including:

- **Business flexibility**—Businesses may want to provide flexibility to an already established workforce to try a new location or to establish a beachhead in a new market. Space is also being leased to accommodate project teams with a fixed and relatively short lifespan. Options include short term (month to month), medium term (6 to 18 months) and long term (greater than three years).

- **Reduce capital expenditures**—While the end-user ultimately pays the amortized costs of the fit-out, they won't be paying for all of it up front. Nor will they be paying for it all at once. This financial feature offers an additional layer of flexibility to the end user and helps shed risk.

- **Participate in creative environment**—Traditional corporate environments can be stale. Small offices frequently are considered uninspiring, lacking the dynamism of larger hubs. A well-established body of academic research (Becker and Sims of Cornell University and Haynes of Sheffield Hallam University, among others) and commercial surveying (HOK, Gensler, Steelcase and Hayworth) concludes that a diverse environment cultivates innovation and productivity.

- **Access innovation/start-up community**—Similar to the above, firms want to be close to innovators and start-ups, both to benefit from their ways of thinking and to potentially invest in them. Both incubators and accelerators[2] utilize flexible workspace, and firms, by extension, should want to as well.

- **FASB/IASB 13 changes**—New accounting regulations requiring firms to disclose real estate lease obligations will increase the visibility of a firm's real estate strategy—and increase pressure on corporate real estate departments to optimize portfolio performance, allowing previously inefficient or unused space to become functional and accountable to the company's bottom line. These changes should benefit the flexible workspace sector, compelling companies to take less core space than with traditional long-term leases. Instead, they will rely more on flexible workspace operators to provide the space to accommodate temporary headcount swings. Occupiers will also increasingly rely on either a landlord or an operator to provide access to amenity spaces. These spaces include meeting rooms, training facilities and breakout areas.

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[2] https://www.ft.com/content/1ea7d6e6-88dd-11e7-afd2-74b8ecd34d3b

Traditionally, incubators are selective and provide indefinite access to co-working space, usually for a fee, along with some mentoring or training. They are often funded by the public sector or academic institutions, and have a strong presence in the life sciences sector as well as digital technology.

Accelerators are intensive fixed-term programs with the aim of scaling up an established business. They can include workshops, mentoring and opportunities to pitch to investors. They might also offer funding in the form of grants or loans, sometimes provided in return for equity in the start-up, or they might charge an upfront fee. Incubator and accelerator services can overlap.

On the other hand, some research might give firms pause when they consider adopting the flexible workspace model.

- **People actually tend to interact less in a shared space,** or discuss business matters face to face, according to a Harvard University study.[3] On the basis of two field studies of Fortune 500 multinational corporate headquarters, the authors found that modern open office architecture decreases the amount of face-to-face interaction by about 70%, while increasing electronic communication by the same percentage. Thus, shared space may not actually facilitate communication.

- **Not all workers are extroverts or thrive in an extrovert culture.** The same Harvard study finds that taking away workers' personal space and placing them in a "fish tank" makes some of them uncomfortable, causing them to withdraw into their electronics.

- **Flexible workspace could be "overstimulating."** Finally, the Harvard study notes that too much information, too many distractions and too many people milling about "appears to have the perverse outcome of reducing rather than increasing productive interaction." A study at the University of California, Irvine found that it takes an average of about 23 minutes to return to your original task after an interruption.[4] Which means companies could be paying less for the space, but ultimately getting less out of their workers.

However, as the number and range of coworking spaces expands, we expect that more firms of every size will recognize the benefits of the approach and deployment will become more culturally acceptable among front line managers and workers.

[3] Ethan S. Bernstein, Stephen Turban, "The impact of the 'open' workspace on human collaboration." The Philosophical Transaction of the Royal Society B, 2 July 2018.

[4] Gloria Mark, Daniela Guidth and Ulrich Klovke, The Cost of Interrupted Work: More Speed and Stress," Univiersity of California, Irvine, School Information & Computer Sciences.

USING FLEXIBLE WORKSPACE TO ATTRACT THE BEST TALENT

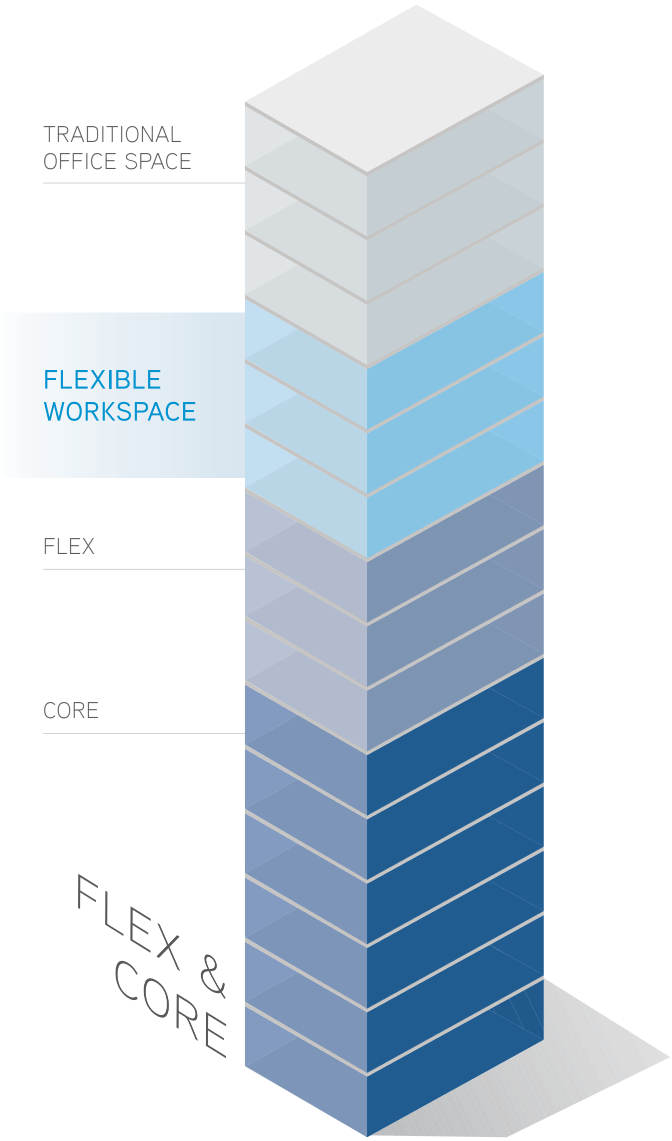
Finally, the growing "talent wars" provide a final important incentive for utilizing flexible workspace. Traditionally, firm locations were governed by location of senior executives, and the rank and file workers followed. The logic is now reversed: corporations are now going to where the young talent is instead. With companies in intense competition to attract the brightest minds, they must be creative about their working space to draw them in, with amenities that appeal to younger workers.

EXPERIENCE MODELS

Flexible workspace operators are providing different types of space to serve different types of occupiers, breaking down into three basic environments:

- **Executive suites/traditional**—As the name suggests, this is the most traditional type of space with separate offices connected to a shared communal amenity area. Regus has long been the leader in this format.
- **Hotel curated**—Extremely high-end space and services are offered here. Suitable for C-suite users, these spaces cater to both individuals and organizations needing to provide a level of amenities on a global scale for executives who travel often. Though there is no leader globally in this space, the focus here is an avoidance of the cookie-cutter feel while maintaining a consistent experience across locations.
- **Mainstream Coworking**—While encompassing a wide gamut, these types of spaces are communal in nature, designed to have a high worker density, and offer physical flexibility, in which desks and offices can be moved around. WeWork is dominant here, although it does provide other models based on client preferences.

ALTERNATIVE LEASING MODELS – FLEX & CORE AND CITY CAMPUS

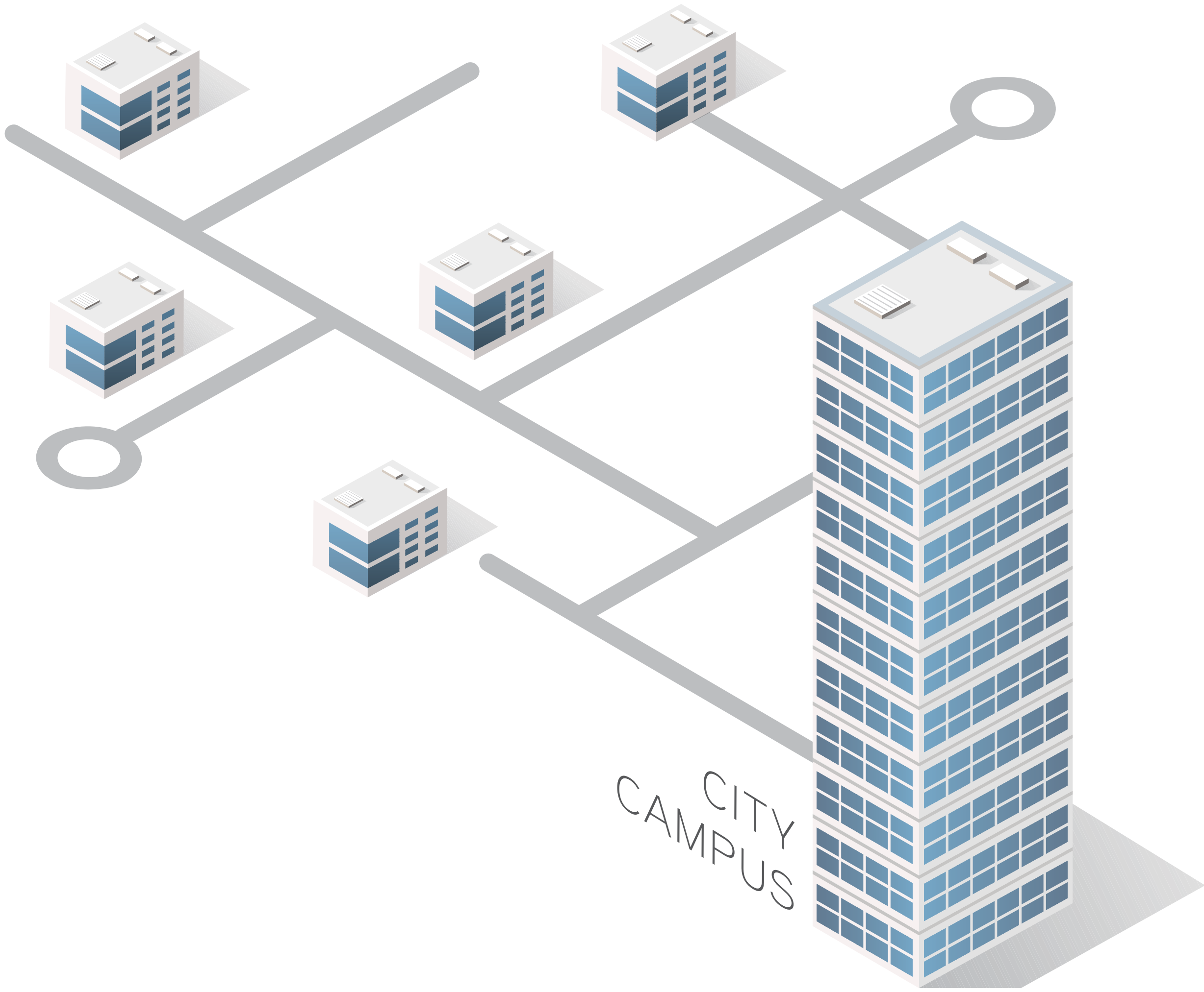


The workplace is increasingly becoming more digital and mobile. There is a growing corporate need for flexibility and an efficient way to work with leasing accounting changes. As a result, three major alternative leasing models are growing in popularity:

Flex & Core

An occupier takes space on a long-term lease for their core operations together with flexible workspace to accommodate volatility in headcount. Variations typically revolve around how the core space is accommodated, either with an operator or directly with a landlord on a traditional lease. Cost savings can be achieved when an operator takes down a large amount of space and passes a portion of the discount to the tenant. Similarly, the coworking provider can achieve economies of scale on fit-out and yield lower effective costs for the tenant relative to traditional leases. Finally, the dollar value of flexibility, mobility and the opportunity to flow capital expenditures through the term as operating expenses means that this leasing model is becoming increasingly attractive.[5]

[5] Colliers International The Flexible Workspace Outlook Report 2018 – APAC



City Campus

Allows businesses with a mobile workforce to access drop-down space across a city, or even globally, depending on the nature of the business. While this has been adopted cautiously so far, we expect this model to be extremely popular with sales and other client-facing teams.

The premise is straightforward: a business consists of a main headquarters and satellite locations but reduces its physical footprint. This enables it to place a percentage of its staff onto a digital platform that grants hot desk or even private office space. This agreement can span across multiple locations within a flexible workspace operator's portfolio.[6] The success of this model will be largely geared around the strength of the flexible workspace operator's digital platform and its ability to link with existing businesses on planned technology. It also depends on the operator's market coverage. Therefore, as operators scale to gain coverage, the attraction of the model is amplified.

Suburban

A variation on the city campus model but situated in well-located suburban nodes that offers both transit access and more walkable districts. These locations can complement the city locations to offer greater flexibility to workers. The providers in this space thus far tend to be smaller and more regional.

[6] Ibid

ISSUES AND OUTLOOK

Notwithstanding the 30-year legacy of IWG/Regus' executive suites model, the modern conception of flexible workspace really only took hold less than a decade ago with the launch of WeWork. With so little history, and so much of the inventory growth so recent, little is known about the impact on the broader office market—or its performance over the course of the business cycle.

In this section we consider several key questions about the coworking model:

1) HOW IS FLEXIBLE WORKSPACE IMPACTING THE OVERALL OFFICE MARKET AND TRADITIONAL LEASING MODELS?

On the surface, the impacts would seem to be small. Our analysis here shows that coworking's footprint is still quite insignificant—only 1.6% of all office space in the markets we surveyed. And even this modest ratio undoubtedly overstates its share of the overall U.S. office market as penetration of this concept is even lower in the secondary markets we did not survey for this study.

Yet, its profile is growing rapidly, as we also explained: virtually 50% building area growth in the last 18 months alone. And its share of recent leasing has been far greater—equivalent to almost a third of the office inventory added over the past 18 months.

But even these figures belie the full impact of flexible workspace on the broader office markets. WeWork is now the largest single tenant in Manhattan, recently displacing J.P. Morgan, and became the top tenant in London a year ago. In many of our top office markets, coworking providers vie with tech tenants for the sectors now leasing the most space—more than law firms, investment banks and other major traditional uses of office space. This degree of concentration gives flexible workspace providers enormous bargaining power when negotiating their master leases.

This influence extends beyond just the coworking leases themselves. There are signs that the flexibility and service offerings typical of coworking agreements are now being felt even in more traditional office leases. Tenants are demanding—and in many cases receiving—shorter and more flexible lease terms. While this is not for everyone or every facility, it is becoming increasingly prevalent, especially for growing or more volatile divisions. Meanwhile, more landlords are offering common amenities like yoga rooms, free food and tenant parties.

2) WHAT ABOUT FLEXIBLE WORKING'S IMPACT ON BUILDINGS THEMSELVES?

With coworking firms one of the few sectors still gobbling up large amounts of space, most landlords should eagerly welcome their business, even if it does represent a form of in-house competition.

But this occupancy comes at a cost. Most important are issues associated with the much greater population density of coworking firms compared to more traditional tenants. Office densities vary significantly by industry and generally have been coming down in recent years as firms seek more efficient floor plans to economize on their occupancy costs. At one time, firms typically leased 225-250 square feet per worker, but many firms have dropped that ratio to 150-175.

But that is still only one-third of the population density in a typical flexible workspace environment, which averages just 60 square feet for person. Housing a population with three or four times as many workers per floor compared to typical tenants just a few years ago places a tremendous burden on the building's infrastructure: elevator waits get longer, the HVAC system requires more energy to cool the building and wear and tear on the carpets and floors is greater.

There can also be more subtle operational impacts. Many flexible workspace operations attract unconventional workers who may not provide the image desired for more conventional office buildings. Even considerations as minor as dog clauses could now be a major lease negotiation. For example, new media and tech companies tend to encourage office dogs, which could lead to extended language on the lease. Issues of control and liability include avoiding the office turning into a kennel, health code violations, general distractions and employee safety.

It is expected that there will also be an impact on property appraisals as the real estate industry considers how to underwrite income streams from flexible workspace providers. In the U.K, the Royal Institute of Chartered Surveyors is working on a position paper addressing this issue.

3) THE "GIG ECONOMY" MEANS LESS OVERALL OFFICE SPACE NEEDED

Firms are providing less space per worker. But firms are also providing space to fewer workers overall. More individuals are actively seeking temporary or contract jobs—popularly known as the "gig economy." And a growing share of firms are contracting out more of their assignments rather than hiring workers directly. Firms appreciate the flexibility of contracts for scheduling projects, while not having to provide benefits. And the contracting firms frequently do not provide office space to their contract workers. Such workers are perfect candidates for flexible workspace even if they can afford to work out of their home. Thanks to advances in technology, millennials especially don't have as strong an attachment to working in a headquarters office when work can be performed from almost anywhere.

Might the availability of flexible workspace encourage a greater shift to the gig economy and outsourcing by making those working arrangements more viable? Would that hasten a decline in traditional office leasing? In this way, coworking space not only pulls tenants from conventional space directly, but also indirectly reduces office leasing by facilitating the gig economy.

4) WHERE DOES FLEXIBLE WORKSPACE GO FROM HERE? NEW PRODUCTS AND PARTNERSHIPS

Coworking is morphing and evolving into different directions, as might be expected in such a nascent industry. New models are emerging, with varying levels of service and flexibility, and targeting different tenant populations. WeWork now has an enterprise division focused on serving the needs of larger corporations, and another targeting mid-sized companies.

Another evolution in coworking: niche spaces that cater to specific businesses and clients. A growing number of specialty players are entering the market, catering to specific industries like biotechnology or construction. This could especially benefit people who are looking to network among like-minded associates in flexible spaces. Niche coworking could include spaces for yoga enthusiasts, musicians, seniors and the LGBTQ community, among others. Amenities could include workshops, seminars, networking sessions and shared equipment and career tools.

But specialized spaces could invite controversy as well. In New York, The Wing offers a women-only membership policy, largely inspired by the #MeToo movement. The space has proven to be a great success, but it's also being investigated by the New York City Commission on Human Rights. That's due to limiting its membership to women only, which is not in compliance with New York's public accommodation law. The ACLU reports that calling a club private does not necessarily make it private, nor does it deserve special attention. The space may be violating anti-discrimination laws, but the jury is still out at this time.

With success comes more competitors, not just from new pure players, but from major landlords and service providers. Tishman Speyer, one of the world's largest private landlords, has launched its own flexible workspace brand, Studio, at its 600 Fifth Avenue location, with immediate plans to several other markets in the U.S. and abroad. Equity Office has partnered with coworking firm Industrious to operate space in some of its properties, while Boston Properties has unveiled its "FLEX by BXP" concept. Other landlords planning flexible workspace operations include Hines and Silverstein Properties, among others.

As coworking matures and its reach widens, merger and acquisition activity among providers is expected. In order to expand and enhance user options while capitalizing on economies of scale, developers, investors and coworking firms are looking to snap up networks and leverage current providers to operate space within existing and new developments. As local operators outside the major markets establish themselves, leading providers could acquire them to expand their networks.

5) WHAT HAPPENS TO FLEXIBLE WORKSPACE IN A DOWNTURN?

Expectations are building that we are nearing the end of this long business cycle, with economic and job growth likely to slow markedly next year and perhaps turn negative by 2020. A key question facing the office sector is how flexible workspace will fare during a downturn.

WeWork and many of its competitors are still loss-making start-ups: WeWork lost $723 million during the first half of 2018, while it earned $764 million in sales; in 2017, it recorded a loss of $933 million, and so would seem to be especially vulnerable to a sudden, significant decline in revenue. How likely is that? Given the short history and lack of track record of this new industry, no one can say for sure. But their business model of generally short tenant leases and a tenant base heavy in individual entrepreneurs and small, thinly-capitalized start-ups, would seem to make for a more volatile cash flow in the event of a recession, compared to traditional landlords who opt for longer lease terms with higher-credit firms who are better positioned ride out the downturn.

Moreover, coworking firms tend to enter long-term leases with landlords but rent out their spaces for relatively short terms. Thus, they would be vulnerable in a downturn if their rents are fixed while their achievable revenues decline due to falling rents in a recession.

On the other hand, flexible workspace operators would benefit in a downturn if tenants could rely more on short-terms leasing blocks of coworking space as needed rather than committing to longer-term, less flexible traditional office lease. Indeed, as we have seen, coworking providers are increasingly targeting larger firms, in part to diversify their revenue base with better-capitalized tenants. In this way, flexible workspace operators can maintain their occupancy through the cycle, though likely at the cost of lower rents as market conditions soften. Time will tell.

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