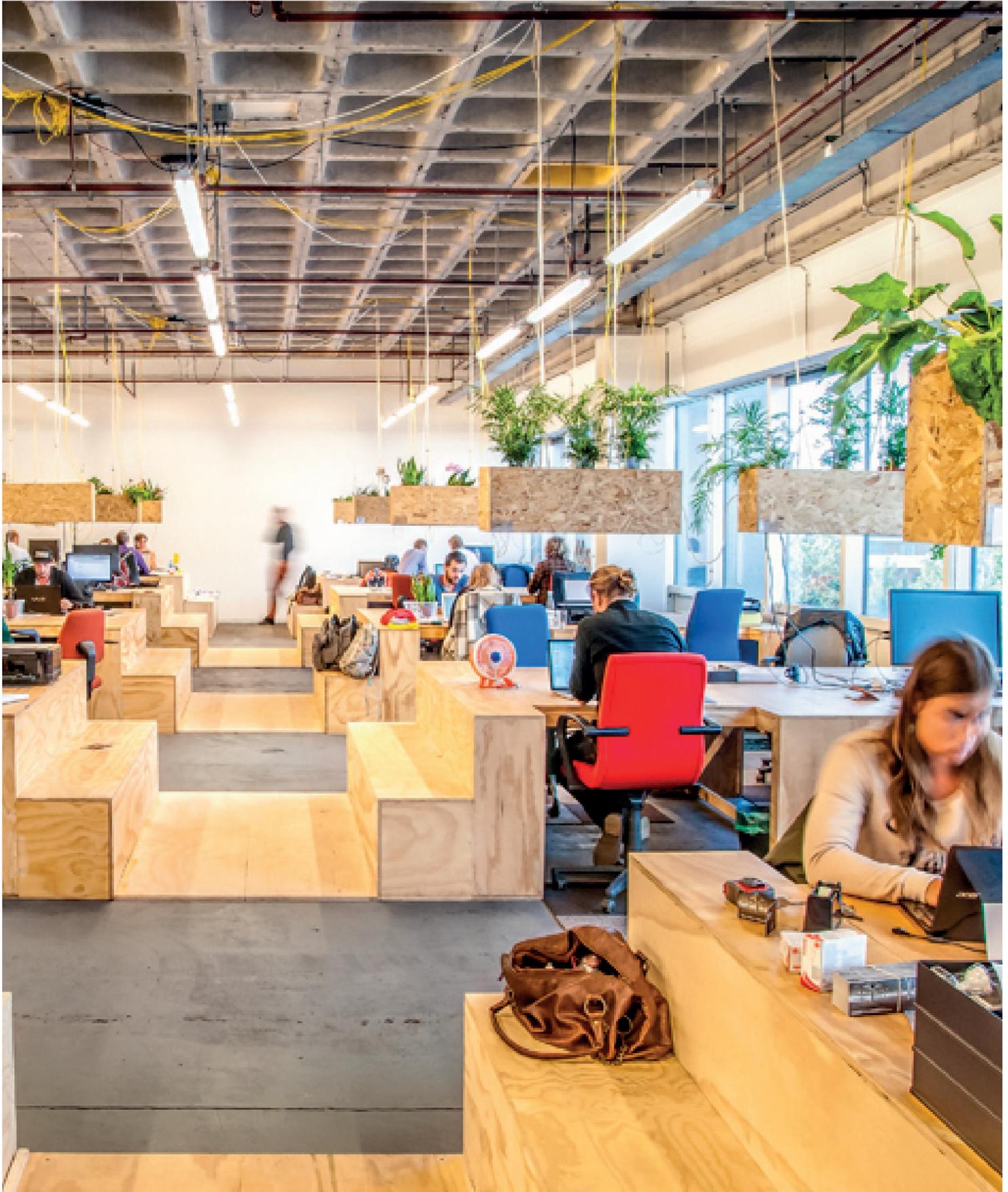


Flexible Office Space



👉 The flexible office market continues to go from strength to strength and its irreversible impact on the overall workspace has secured its position in the long term 🏆

FLEXIBLE OFFICES GOING STRONG

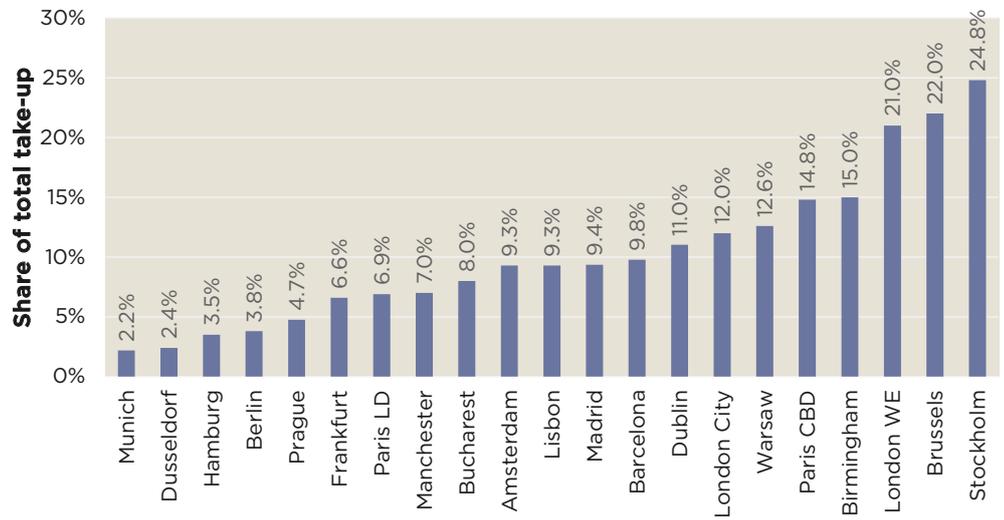
The flexible office market continues to go from strength to strength and its irreversible impact on the overall workspace has secured its position in the long term. However, there are question marks over the sustainability of the serviced office sector due to its rapid renaissance over the last five years.

We believe that there are a number of factors that will impact the flexible office market as we continue to see the office sector as a whole evolve and adapt to the growing trend for the workplace to be viewed as a service. Experience, flexibility, wellbeing and talent attraction and retention are of paramount importance to tenants and for flexible office space operators these values are in the epicentre of their strategies.



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Share of flexible office space take-up in 2018 was close to 10% of the total



Source: Savills Research

European flexible offices

2018-2019 trends and hotspots for the next two years

Flexible office space take-up was up in 2018

2018 saw the co-working and flexible office sector maintain its position at the forefront of the office market conversation with a particular focus on its stellar growth and its future prospects. Last year flexible office space (FOS) take-up increased by 20% yoy to reach almost 830,000 sq m across the 20 major cities that we monitor. This corresponds to 9.9% of the total take-up levels, when only three years ago this share was below 3%. The cities where the sector has matured the most are Stockholm (24.8% of total take-up in 2018), Brussels (22%), London (15.6%) and Paris CBD (14.8%). Double digit shares were also achieved in Warsaw (12.6%) and Dublin (11%).

Volumes were down in the core markets

The largest markets in terms of volume were London (184,000 sq m), Warsaw (108,550 sq m) and Brussels (80,000 sq m), while the markets with the largest annual

rise in take-up were Bucharest (almost 9 times higher), Brussels (6x) and Warsaw (3.5x). At the same time FOS take-up dropped by 40% yoy across the German cities, by 10% in London and by 7% in Paris. In Germany the share of activity remains relatively low, below 4% of the total. This could be attributed to strong economic fundamentals, which have been driving traditional occupier activity over the past few years and left the market with very low supply of office accommodation.

Outlook

In the short term, the risk of slowing economic growth and reduced occupier demand could bring some challenges to flexible office operators, nevertheless, in times of uncertainty we expect occupier demand to shift ever more towards shorter leases and elastic space requirements, in order to maintain the advantage of adaptability in case of a downturn. In 2018, while the overall take-up was 2% down yoy, mainly due to lack of availability, FOS take-

up was up by 20% yoy. In 2019, Oxford Economics forecasts more than 155,000 new service sector jobs across the cities we monitor. These can overall sustain the current levels of demand for FOS and in some cases exceed them.

Looking forward, we, expect the popularity of the sector to intensify as it diversifies its offer. We believe that cities with dynamic economies, which attract innovation and talent can see demand for flexible offices rise up to 15% of the total in the medium term, while in the long term this could increase to 20-25% of the activity, especially in periods of economic growth and business investment.

Over the next two years we expect to see the highest expansion of flexible offices in smaller but dynamic markets where availability allows and the share of FOS take-up is still below 15%, such as Dublin, Warsaw, Madrid, Barcelona, Bucharest and Lisbon. In the following section we discuss the drivers of this trend.

9.9%

The share of flexible office take-up in European hotspots for the whole of 2018



Last year flexible office space take-up increased by 20%



Flexible office space take-up reached c. 830,000 sq m across 20 cities in 2018



In Stockholm Brussels and London West End 2018 take-up share was above 20%



Flexible office space share can increase to 15% of take-up over the next two years



The expansion of flexible offices is constrained by lack of available space in some cities

Hotspots for flexible office space demand

We have identified the cities where we expect demand to grow the strongest based on a set of criteria related to economic growth, job creation, innovation, and property market fundamentals. We have assumed that demand for this type of space will be stronger in cities with better economic prospects and future employment growth, which have been attracting rising amounts of VC investment and where talent can lead innovation. Markets with sizeable office sector activity already attract a diverse occupier base with large number of SMEs and freelancers, while in places with long leases demand for flexibility can be of higher importance. The actual growth of the sector, will be conditional to space availability.

It is no surprise that **London, Paris and Berlin** are at the top of the ranking, as they attract 80% of the VC investment in Europe (cities covered in this report),

which indicates a future need of flexible office space for many of the start-ups that will emerge from this activity. In London and Paris the share of flexible office take-up is already amongst the highest in Europe (London WE 19%, London City 12%, Paris CBD 15%). In Berlin however it is still at 4% and with an overall office vacancy rate of 1.5% there are limitations in the potential of the immediate expansion of the concept.

Dublin and Stockholm rank third and fourth because of positive economic growth prospects and job creation. Long leases and expensive rents have shifted some occupiers towards more flexible property solutions and they are already dynamic FOS markets (11% and 25% share of take-up respectively). We believe that Dublin has good prospects for further expansion, while Stockholm may be restrained by lack of available space.

Warsaw, Frankfurt, Amsterdam and Hamburg, have experienced significant rise of VC inflows over the past decade, which

brings them in the top ten of the ranking of cities where demand for flexible offices is on the rise. In Warsaw and Amsterdam the share of FOS take-up has already reached 13% and 9% respectively last year, while in the German cities it has been growing more slowly and was at 7% in Frankfurt and 4% in Hamburg in 2018. Significant increase of VC investment since 2009, although starting from a low base, was also noted in **Lisbon**, which ranks lower (16th) overall due its small market size. FOS share of activity was at 9% last year and expected to rise further.

Employment growth prospects for the regional UK cities are positive, and flexible offices may be a good way to bypass the long leases in the market. Last year's share of FOS take-up was at 15% in **Birmingham** and 7.0% in **Manchester**.

Brussels, ranking 10th, has seen significant rise in the supply of flexible offices and is a market where the concept will continue to expand, as lease lengths are long

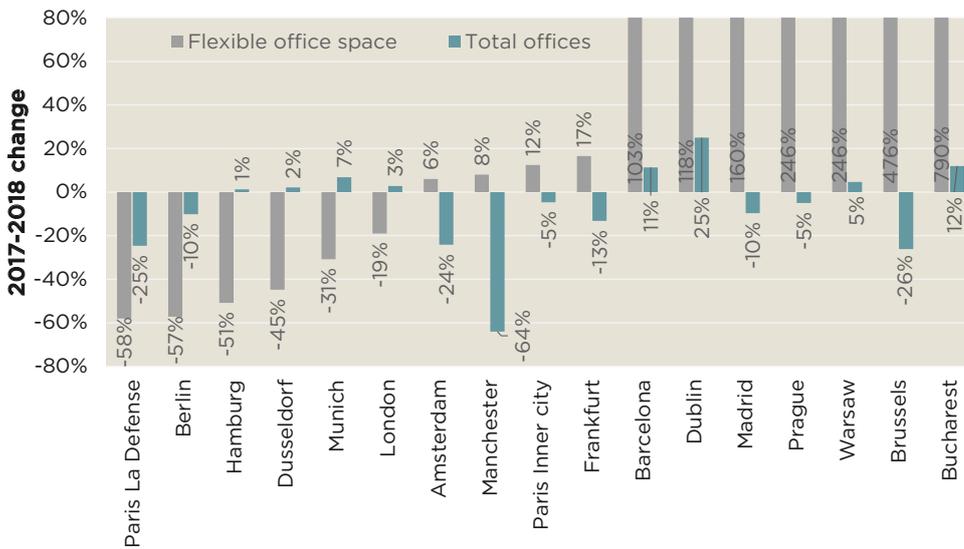
Flexible office space demand: European hotspots for 2019-2020

Rank	Location	Flexible office space demand score	2018 share of flexible office space take-up	2018 total vacancy rate
1	London	8.0	14.6%	4.9%
2	Paris	7.0	11.0%	3.0%
3	Berlin	6.1	3.8%	1.5%
4	Dublin	6.0	11.0%	8.1%
5	Stockholm	5.9	24.8%	3.5%
6	Warsaw	5.7	12.6%	8.7%
7	Frankfurt	5.6	6.6%	7.0%
8	Birmingham	5.4	15.0%	11.1%
9	Amsterdam	5.3	9.3%	5.1%
10	Hamburg	5.3	3.5%	4.4%
11	Brussels	5.2	22.0%	8.0%
12	Madrid	4.9	9.4%	9.8%
13	Barcelona	4.8	9.8%	5.4%
14	Bucharest	4.7	8.0%	7.0%
15	Manchester	4.7	7.0%	9.7%
16	Lisbon	4.0	9.3%	8.0%
17	Munich	3.8	2.2%	2.4%
18	Prague	3.4	4.7%	5.1%
19	Dusseldorf	2.6	2.4%	6.9%

Source: Savills Research

It will require more transparency from providers on occupancy levels and rates achieved, in order to measure the performance of the sector and create investor confidence

Flexible office space take-up 2017-2018: Flexible office take-up increased in the majority of locations, despite the decrease of total office take-up



Source Savills Research

and there are several activities supporting the European Union that can benefit from short and flexible leases.

Madrid is a sizeable market, with growing economy and employment, which has also experienced a growth of flexible offices, capturing 9% of take-up. **Barcelona** benefits from above average employment creation prospects and FOS activity was at about 10% of total last year, reflecting a dynamic local economy. We expect demand for this type of space in the two large cities of Spain to continue driven by SMEs and start-ups.

Flexible offices are expanding in **Bucharest** (take-up at 8% of total last year), which is a cheaper location, in terms of property and labour costs and a growing economy. Despite the relatively low VC volume, there is an increase observed. Same trend is observed in **Prague** too, which suffers of lack of supply of quality office space. FOS take-up was still at 5% of total last year but expected to rise.

Flexible office trends to watch for 2019

Globalisation, consolidation and specialisation

1 Globalisation of providers

Businesses are increasingly scaling to new markets and territories and therefore the flexibility to allow this is becoming increasingly important for providers, the ability to offer customers multi-global locations can be a powerful selling point and differentiator. Last year we saw TOG announce its first European location in Frankfurt, Knotel enter the London market and The Brew tie up with German provider Rent24. We expect more and more providers to scale their business into new territories in 2019, in particular more US names entering Europe, UK ones establishing a presence in key European cities such as Dublin, Berlin, Frankfurt and Paris, and the US and more Asian providers coming in to Europe and the US.

2 Growth of niche

For a while now we have seen tech and innovation-only co-working spaces such as Huckletree, Techspace and Runway East in London who screen applicants to curate a community of like-minded businesses. However, given the current competition of different spaces in the market, we expect more new providers to focus on a niche in an effort to differentiate themselves. We are already seeing the emergence of female only co-working spaces, but we expect more spaces to focus on sector niches such as retail and fashion, food

and businesses with a social purpose. In addition, there has been an emergence of spaces offering a niche facility as a means to attracting clients, the big trend we expect in 2019 is the growth of the on-site crèche or nursery for parents to work whilst their children are looked after. Thirdspace and Cuckooznest have started the trend in London and we expect more providers to follow suit, especially as the flexible providers grow into more residential areas.

3 Rise of the co-working landlord

There is no question the landlords have woken-up to the world of co-working, but only a handful have really jumped in and actually delivered their own space, such as British Land with Storey, Legal and General with Capsule or Blackstone with Yourspace at Chiswick Park. We anticipate that 2019 will see a surge in the number of landlords delivering their own flexible office product as part of a wider office scheme as they seek to compete with the co-working market as tenants continue to seek flexibility and service. The challenge for landlords will be the service and hospitality element. For the providers it's not about just providing a space and collecting rent, they go above and beyond to ensure that businesses thrives in the space they occupy.

4 Consolidation

Given the number of new entrants into the serviced and flexible office market, there has been an inevitable growth in competition on pricing, particularly in London, and we expect to see some winners and losers with a rise in consolidation between providers. Deskmag reports that 40% of co-working spaces do not make a profit, this is a significant number and, given the continued rise in competition, for many this is not likely to be sustainable. Providers at risk should pay particular attention to who their core customer base is and what type of space they want. Often we see providers seeking to scale too quickly or develop a product that doesn't meet their market demand and this is when they can come into trouble.

5 The hope for transparency

There is still much scepticism around the serviced office sector from those outside and in order for the sector to be taken more seriously as a mainstream sector from a valuation and investment perspective, it will require more transparency from all providers on occupancy levels and rates achieved.



Workthere

Workthere is a business by Savills focused solely on helping businesses find flexible office space, whether that's a serviced office, co-working or shared space.

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Savills Commercial Research

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