COLLIERS INSIGHTS

OCCUPIER SERVICES | EMEA | OCTOBER 2020

Colliers INTERNATIONAL

FLEX FORWARD

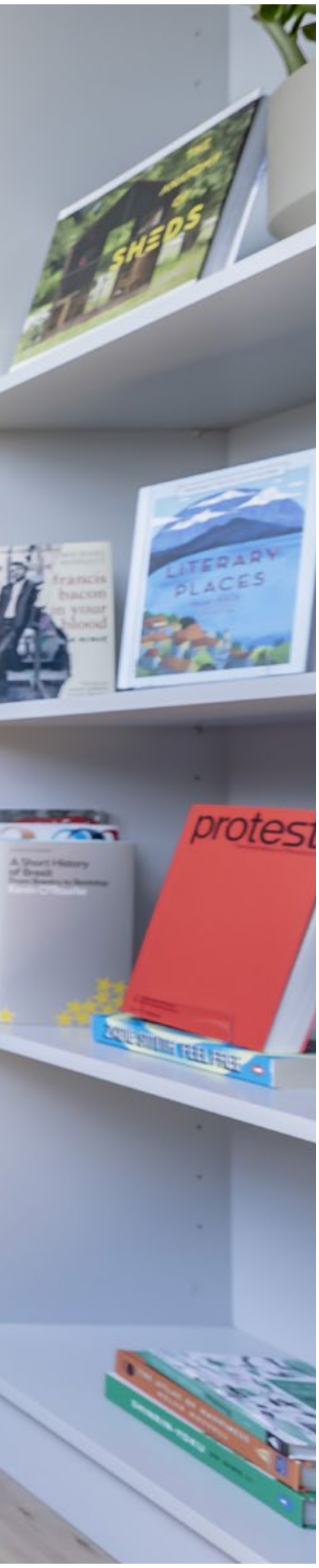
THE FLEXIBLE WORKSPACE REPORT 2020

EMEA

FORA | LONDON

COVER IMAGE: PLATF9RM | UK

INTRODUCTION



The COVID-19 pandemic has accelerated workplace change and confirmed that work is no longer a place but an activity. Millions of people across EMEA have been forced to adapt their working patterns and employers are navigating how remote working can make up part of their workplace strategy - decades of change have been squeezed into months.

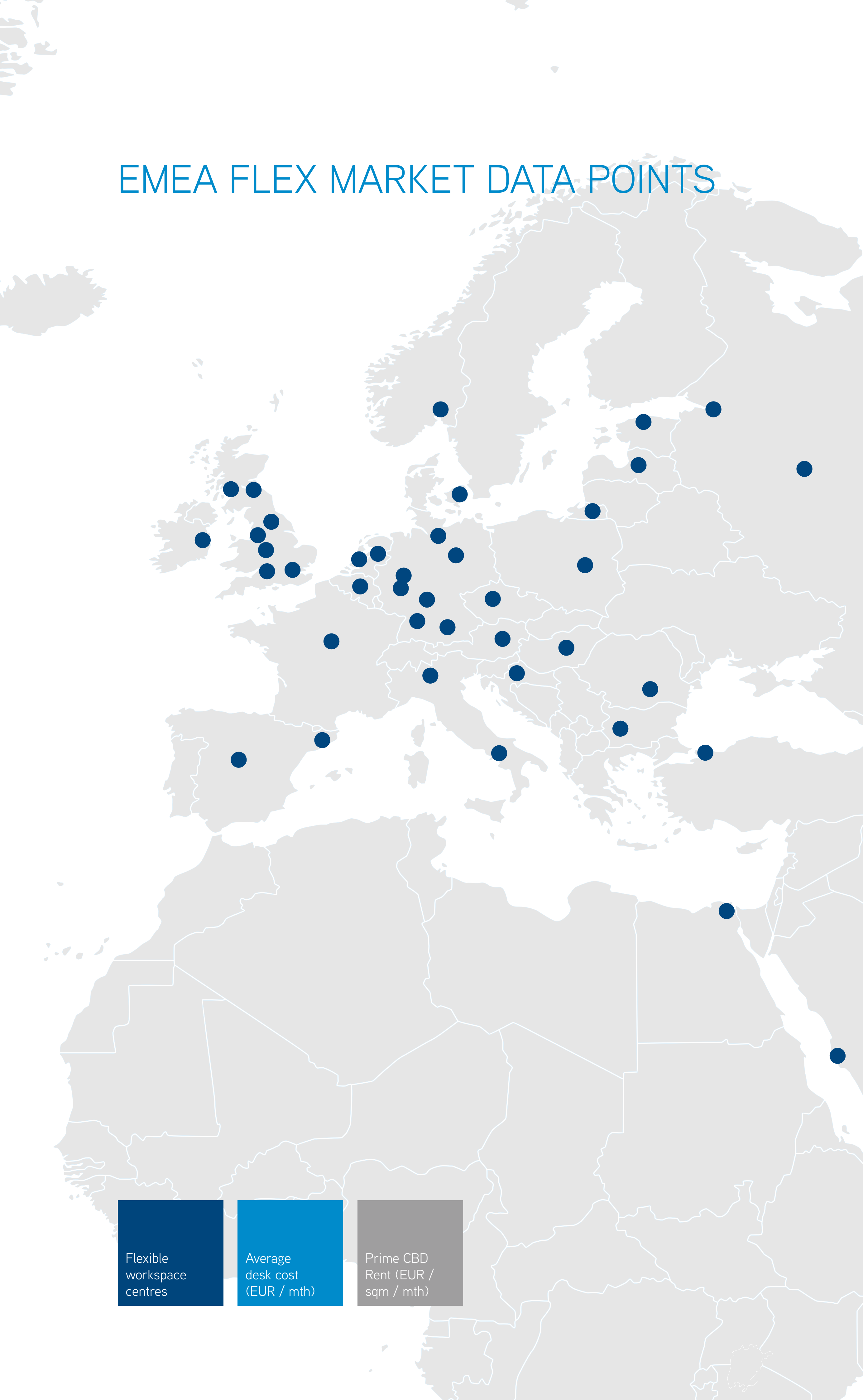
The flexible workspace sector has not been immune to the effects of the pandemic but there are signs of positivity across EMEA, with some operators reporting solid performance and considering expansion opportunities. As enterprise occupiers evaluate their real estate decisions and adjust their strategies, we expect the flexible workspace sector to be at the forefront of many new solutions. Looking back at our **predictions for the sector** in January, the pandemic has accelerated many of these forecasts. This report illustrates some of the strategies available to enterprise occupiers to manage the "new normal".

Asset owners across the region are increasingly interested in having exposure to the sector, not just for flexible workspace but also for the range of other services and amenities they can offer. This report evaluates different delivery mechanisms to integrate flexible workspace into assets and the implications on valuation.

On the following pages we start with a deep dive into major markets across EMEA, analysing how the sector has performed over the last 18 months, before we guide you through occupier strategies, models and considerations for asset owners.

TOM SLEIGH
Head of Flexible Workspace Consulting | EMEA

EMEA FLEX MARKET DATA POINTS



AMSTERDAM		
141	500	
BARCELONA		
109	550	
BERLIN		
119	1,67	
BIRMINGHAM		
22	410	
BRISTOL		
19	356	
BRUSSELS		
79	1,30	

0	39
0	28
5	40
0	34
5	37
0	26

BUCHAREST	59	330	18
BUDAPEST	59	505	24
CAIRO	80	188	24
COLOGNE	34	800	25
COPENHAGEN	89	805	23
DUBAI	96	1,283	39
DUBLIN	101	750	56
DUSSELDORF	31	800	29
EDINBURGH	16	438	34
FRANKFURT	67	975	46
GLASGOW	14	312	32
HAMBURG	81	950	30
ISTANBUL	45	613	27
JEDDAH	21	1,431	23
LEEDS	25	410	31
LONDON	886	1,204	118
MADRID	101	600	35
MANCHESTER	35	383	37
MILAN	62	944	49
MOSCOW	82	463	67
MUNICH	76	1,150	41
OSLO	58	1,563	43
PARIS	576	1,065	73
PRAGUE	51	763	23
RIGA	21	230	16
RIYADH	28	1,186	32
ROME	38	689	36
ROTTERDAM	43	350	20
SOFIA	48	131	15
ST. PETERSBURG	28	450	26
STUTTGART	26	750	26
TALLINN	16	320	17
VIENNA	65	1,490	28
VILNUIS	19	340	17
WARSAW	70	415	26
ZAGREB	10	231	15

EMEA FLEX MARKET OVERVIEW

COVID-19: THE IMMEDIATE AFTERMATH

Our analysis of EMEA office markets in the first six months of 2020 showed a considerable, but not unexpected, slowdown in the demand for, and new supply of, flexible workspace.

Only about 330,000 sqm of new flexible workspace operations was committed to by operators and landlords across the 42 surveyed markets. This figure is 50% behind the corresponding period a year ago as most operators shed their immediate expansionary plans in response to the outbreak of the COVID-19 pandemic.

TAKE-UP DISPARITY BY MARKET

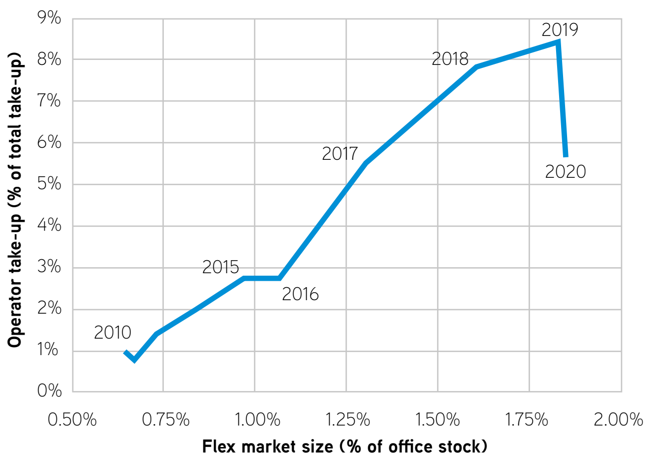
Despite the evident slump in demand and a number of sites ceasing operation across the region, the flexible workspace sector had not lost any of its foothold by July 2020. Where some sites ceased to operate, another 162,000 sqm on new operations were inaugurated during the first half of 2020. This has actually increased the share of the flexible workspace market in H1 2020, on average, to just under 2% of total modern office stock.

The impact of the national lockdowns is clearly visible in activity levels: only about half of the surveyed markets in EMEA recorded any new acquisitions of flexible workspace by July 1. Looking at the active markets alone, it appears that those with lower saturation levels were able to sustain confidence and higher levels of activity. As illustrated in Figure 2, the markets like Hamburg, Vienna, Moscow and St. Petersburg all reported relatively strong flexible workspace take-up levels, ranging between 10-30% of total office take-up.

Markets with higher saturation rates, such as London, Paris, Amsterdam and Berlin remained on the cautious side (with take-up rates below 5%). The focus has been on maintaining operational sites, with particular consideration for the viability of open, co-working spaces in light of physical distancing requirements.

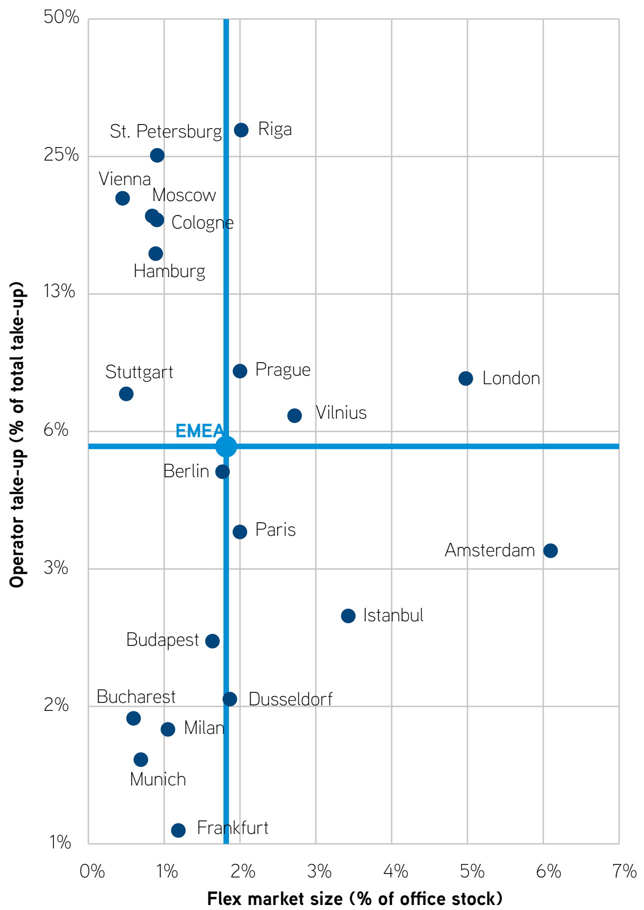
Overall, flexible workspace take-up in the majority of markets (as a proportion of total take-up) remained in the single digits. Many multi-facility operators have opted to carry out a review of their development plans, alongside a strategic review of the businesses, to ensure the financial feasibility of their flexible workspace provision over the long term.

Fig.1: Flexible workspace market evolution, EMEA



Source: Colliers International

Fig.2: Flexible workspace market saturation, EMEA, by Market, H1 2020



Source: Colliers International

OPERATOR DIVERGENCE

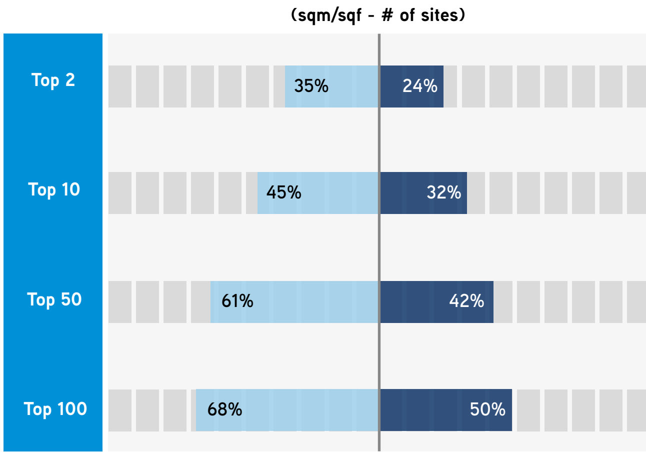
Our survey of flexible workspace operations concluded that as at 1st July 2020 there were 1,300 operators managing a total of 6.0 million sqm across 3,300 sites.

IWG and WeWork remain the dominant parties, jointly controlling one-in-four flexible workspace locations and a third of all space on offer across the markets surveyed. During H1 2020, new space delivered to market by the two dominant players fell to just under 60,000 sqm - in 2019 the two firms set up new operations just shy of 0.5 million sqm. This follows WeWork's review of the sustainability of its global portfolio and subsequently pulling out of a number of existing and/or committed schemes across EMEA - including Milan, Brussels, Vienna, Dusseldorf and Manchester, while abandoning plans to expand into Budapest and Bucharest.

WeWork's decreasing footprint will help re-balance the divergence of ownership and operator activity, but there still remains a significant 'flexible wealth gap'. As we move further down the ownership pyramid, outside of the top two largest operators (by sqm of operated space), who jointly control 24% of sites and 35% of space, the top-50 – predominantly international players – account for 61% of sqm and 42% of sites.

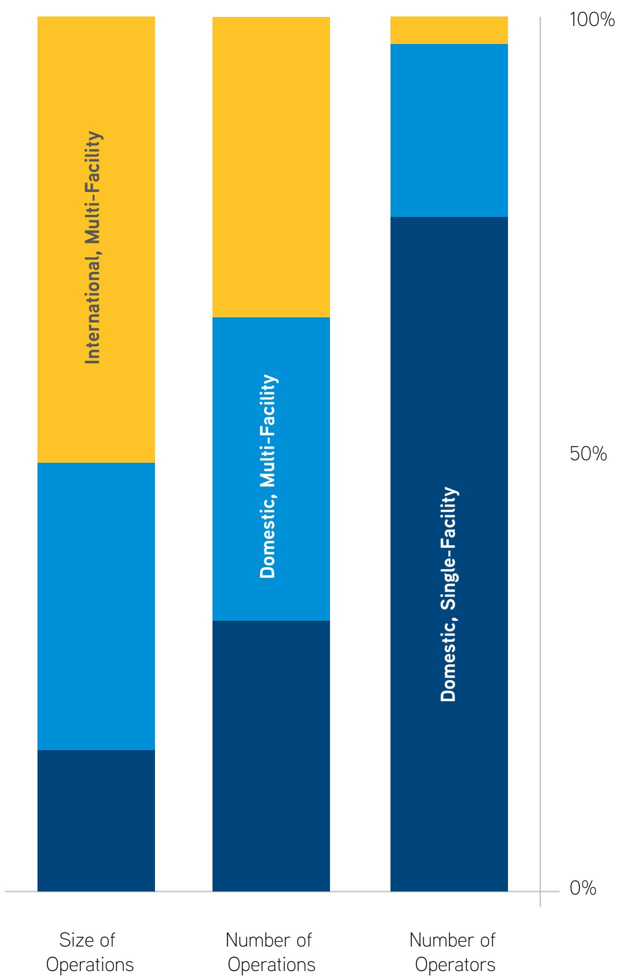
The rest is shared between mostly domestic, independent, single and multi-facility operators. While there were only a low number of cases of single-facility operations closing down due to falling demand from flexible workspace users, the sector's exposure to the current crisis remains high. Without a substantial financial buffer to protect them from such external shocks, and a lack of government support for the SME industry, there will inevitably be further site closures and operators will be subject to increased M&A activity within the sector. Long term sustainable growth, albeit aided by both of the aforementioned, will continue to rely on national, multi-facility operators, forming the backbone of the sector.

Fig.3: Operator market share, July 1, 2020



Source: Colliers International

Fig.4: Operator market share, July 1, 2020



Source: Colliers International

CO-WORKING BECOMES THE TROUBLED CHILD OF FLEX

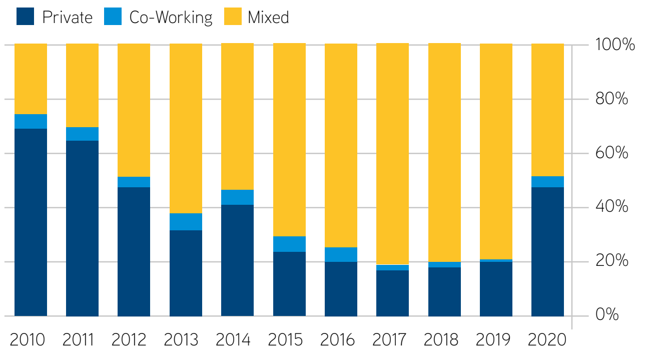
We are yet to see the full impact of the current pandemic and what the new normal will look like post-COVID-19. However, what we have already seen so far in terms of the market reaction is that the open, co-working space has been challenged by a need for low density, fully sanitised workspace. Consequently, we have seen a clear shift towards providers creating more private space (Fig.5) while letting some of the co-working space go.

Our survey found that, on average, 10% of the existing flexible workspace across EMEA is currently set up to service a co-working environment. This space either forms part of larger 'mixed' workspaces that offer a range of space types including private offices, shared desks or hot desks or can be found in pure co-working set-ups. In light of the evolving new normal, this leaves 9 out of 10 flexible workspaces COVID-safe.

Indeed, the bulk of operational closures and downsizing attempts so far involved predominantly co-working and mixed space. These were recorded in locations where co-working as a proportion of the flexible workspace options on offer, was at the higher-ends of the spectrum - this currently ranges between 6% and 18% across EMEA. Closures have also been more frequent in locations where independent, single-facility flexible workspace operators dominate the market (Fig.6).

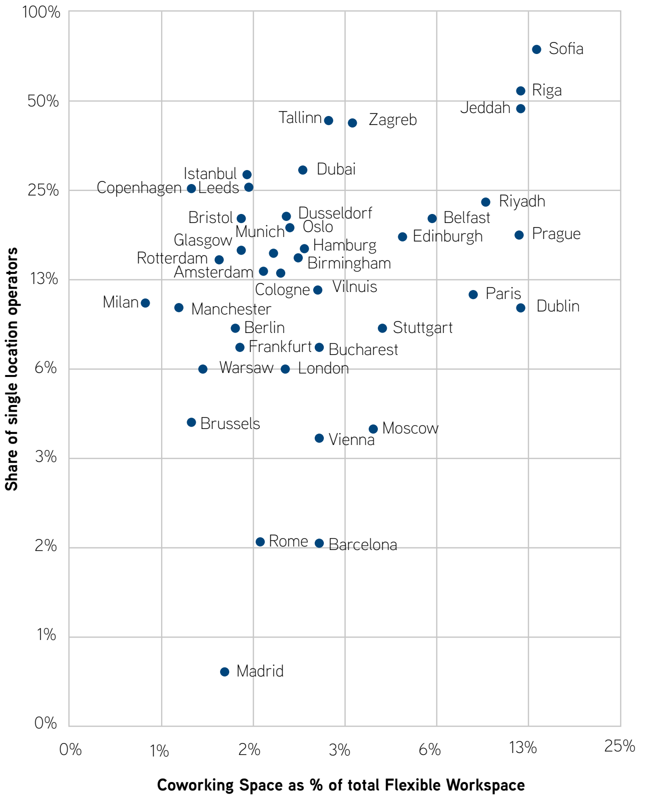
Markets such as Sofia, Prague, Vilnius, Manchester and Hamburg have already seen schemes close, among the first to offload any excess and not viable space. The next 12-24 months will be determined in large part by the amount of working capital that flex operators can put towards upgrading their spaces to future, 'post-COVID' requirements.

Fig.5: Annual supply of Flexible Workspace, by type of space, 2010 – 2020 H1



Source: Colliers International

Fig.6: Covid-19 Exposure Co-working vs Single-facility Operators



Source: Colliers International

SUBURBAN EXPANSION

Most operator demand over recent years has been for central locations, sustaining a heavily CBD focused flexible workspace sector. Up until now, decentralisation had typically been the result of the tight supply of adequate CBD space prompting high-end operators to look further out for viable options.

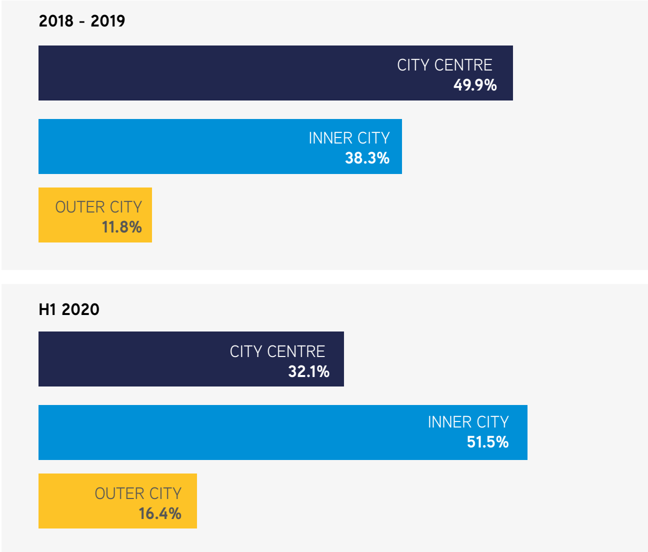
Since the onset of the pandemic, however, it has become increasingly clear that providing secure, flexible workspace within an easy/safe travel distance from home will be key in (re)shaping the market post-COVID-19. What is slightly unexpected however, is to see how quickly operators have reacted to this need, with a shift in interest to non-central and suburban city areas to reaffirm or establish their local presence.

Over the last six months, about 18% of demand across the 42 surveyed markets that has previously targeted city centre locations has shifted to inner city and more suburban outer city areas. While in 2018-19, on average, only 12% of new flexible workspace was acquired in the suburban regions, this has increased to 16% in the last six months. The inner cities have also gained an additional 13%, becoming the most popular location type to date in 2020 with a 52% share of demand.

Evidence suggests that some of the cities most heavily dependent on public transport were the quickest to see substantial activity outside of the CBD: Moscow (84% of flex take-up), Paris (60%), Budapest (100%) or Prague (66%). Other cities, including London, Amsterdam and Vienna saw activity remain strongly city centre focused. Indicating that the flexible workspace market focus is broadening its geographic reach, but it remains to be seen just how it will decentralise per city – if at all.

Whether or not a decentralisation will be sustained, will not be discernible for at least another 12-18 months, as occupiers get to grips with workspace needs and operations during and post-COVID. A snapshot of corporate PR and articles informs us that 25% of companies reviewed are re-considering their flex operations, and/or increasing the use of flexible space options. Around 70% are yet to make any decision on how their occupational portfolio will change. As break clauses are actioned and lease renewals come under review, there is a definite reshaping of the market underway, with the recent changes to date exceeding any margin of error.

Fig.7: Supply of 'pure' Coworking Space, as % of all new Flexible Workspace, 2018-2019



Source: Colliers International

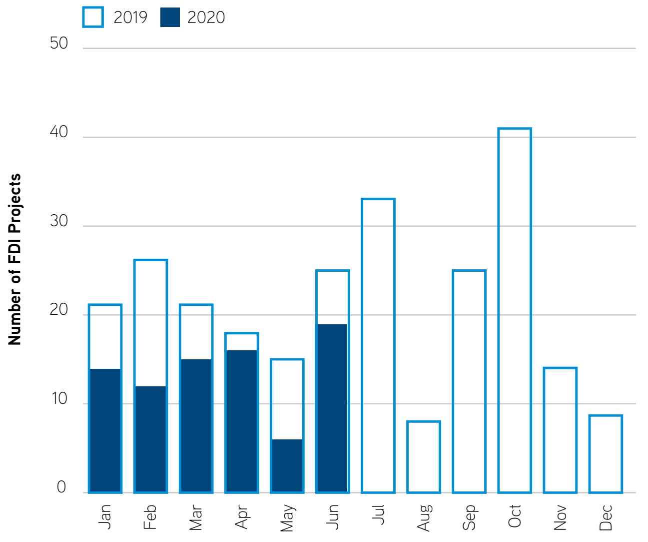
OUTLOOK

The latest figures from FDi Markets suggests only 82 new flexible workspace projects were announced across EMEA in the six months to June. This is down 35% on announcements in H1 2019. Encouragingly however, a weak May was followed by a quick rebound in June (Fig.8) supporting the continued appetite of flexible workspace providers to invest in the sector.

Indeed, the committed pipeline as at July 1 remained in place overall, with the potential to create 1 million sqm of additional flexible workspace, spanning 222 sites in 30 markets over the course of the next few years. Two thirds of this volume are on the books to open before the end of this year, however it is likely that some of these will be pushed into 2021 and/or some schemes abandoned as the reassessment of businesses and portfolios continues. Assuming three out of four schemes do open for business as planned in H2, we expect to see the market expand by another 0.5 million sqm before year end.

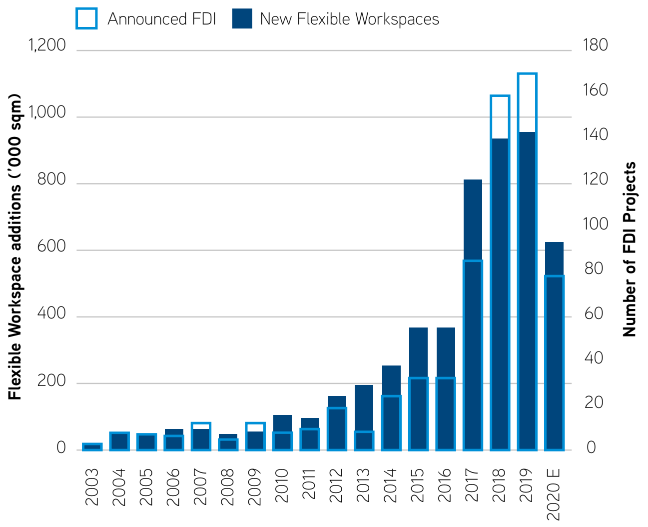
Colliers' 'Working from Home Survey' points to the fact that employees wish to continue to work from home more, but not every day **(click here to see the results of the survey)**, and flexible workspace will form part of the 'third space' workforces will utilise alongside core offices, taken up as enterprise level solutions in a number of possible models, as detailed in our Occupier Strategies section of this report. It is inevitable that the flexible workspace sector will adapt accordingly going forwards, and that the level of adaption and adoption will vary significantly by city. But it is here to stay and will continue to play an increasingly important role in the long run.

Fig.8: Announced Flexible Workspace FDI



Source: Colliers International, FDi Markets

Fig.9: 2020 forecast: Flex take-up & FDI



Source: Colliers International, FDi Markets

KEY MARKET DATA POINTS

	Number of open centres	Number of operators	Flex space (% of office stock)	Flex take-up H1 2020 ('000 sqm)	Total office market take-up	Vacancy rate (%)	Operator take-up forecast 2020	Take-up forecast 2020	Prime CBD rent (EUR/sqm/mth)	Average desk cost, Private office, EUR/mth
AMSTERDAM	141	50	6.1	4.0	118	5.1	▼	⇔	39	500
BARCELONA	109	55	2.9	0.0	85	4.0	▼	▼	28	550
BERLIN	119	42	1.8	16.9	331	1.2	▼	▲	40	1,675
BIRMINGHAM	22	14	4.1	0.0	37	8.0	▼	⇔	34	410
BRISTOL	19	11	3.0	0.0	25	5.0	▼	⇔	37	356
BRUSSELS	79	32	1.1	0.0	184	7.4	▼	▼	26	1,300
BUCHAREST	34	19	1.9	2.0	124	11.3	▼	▼	18	330
BUDAPEST	59	36	1.7	3.6	168	7.3	▼	⇔	24	505
CAIRO	80	69	2.2	0.0	n/a	17.0	▼	⇔	24	188
COLOGNE	34	22	0.9	15.5	85	2.5	▲	▼	25	800
COPENHAGEN	89	56	4.4	12.0	n/a	6.3	▲	⇔	23	805
DUBAI	96	56	1.4	0.0	n/a	35.0	▼	▼	39	1,283
DUBLIN	101	38	3.4	0.0	112	7.0	▼	⇔	56	750
DUSSELDORF	31	18	0.6	2.1	141	5.5	▼	⇔	29	800
EDINBURGH	16	9	2.1	0.0	n/a	n/a	▼	⇔	34	438
FRANKFURT	67	38	1.2	1.5	177	6.9	▼	▼	46	975
GLASGOW	14	8	2.3	0.0	n/a	n/a	▼	⇔	32	312
HAMBURG	81	49	0.9	26.4	175	2.8	▲	▼	30	950
ISTANBUL	45	10	3.5	0.8	35	28.6	▼	▼	27	613
JEDDAH	21	17	1.0	0.0	n/a	18.0	▼	▼	23	1,431
LEEDS	25	18	3.5	0.0	16	7.5	▼	⇔	31	410
LONDON	886	148	5.0	28.4	353	5.4	▼	▼	118	1,204
MADRID	101	30	1.1	0.0	148	8.7	▼	▼	35	600
MANCHESTER	35	20	6.1	0.0	36	10.4	▼	⇔	37	383
MILAN	62	18	1.1	2.3	164	10.0	▼	⇔	49	944
MOSCOW	82	32	0.9	111.5	614	6.0	▲	▼	67	463
MUNICH	76	35	0.7	3.9	326	2.7	▲	▼	41	1,150
OSLO	58	26	1.2	0.0	n/a	5.1	▼	⇔	43	1,563
PARIS	576	63	2.0	22.1	592	5.7	▼	▼	73	1,065
PRAGUE	51	25	2.0	12.5	149	6.1	▼	▼	23	763
RIGA	21	12	2.0	1.9	7	14.1	▼	▼	16	230
RIYADH	28	15	0.7	0.0	n/a	20.0	▼	▼	32	1,186
ROME	38	21	0.7	0.0	42	8.2	▼	⇔	36	689
ROTTERDAM	43	15	3.2	0.0	61	10.7	▼	▲	20	350
SOFIA	48	37	2.3	0.0	56	10.6	▼	▼	15	131
ST. PETERSBURG	28	12	0.5	11.7	58	6.7	▲	▼	26	450
STUTTGART	26	16	0.5	5.8	77	2.2	▲	▼	26	750
TALLINN	16	12	1.6	0.0	n/a	8.6	▼	▼	17	320
VIENNA	65	31	0.9	10.8	44	3.9	▲	▼	28	1,490
VILNIUS	19	13	2.7	2.7	40	3.4	⇔	▼	17	340
WARSAW	70	28	2.9	0.0	335	7.9	▼	▼	26	415
ZAGREB	10	8	1.5	0.0	n/a	5.0	▼	▼	15	231

THE FLEX VALUE PROPOSITION

How occupiers can leverage the flexible workspace sector as part of their Corporate Real Estate (CRE) strategy

There are a number of component parts to flexible workspace and, when considering a corporate real estate strategy, occupiers should consider which components are best suited to their business needs and the level to which they require each component.

SPEED, SHARED

HOURLY / DAILY

Meeting Space

- On-demand meetings
- Off sites / project planning
- Conference / event booking

DAILY / MONTHLY

Traditional Coworking

- Open plan working environment
- Dedicated or hot desks
- Shared facilities

MONTHLY / ANNUAL

Private Offices/Suites

- Private office or suite
- Limited customisation
- Shared facilities

ANNUAL+

Enterprise Solutions

- Dedicated floors/offices
- Ability to customise
- Branding opportunities

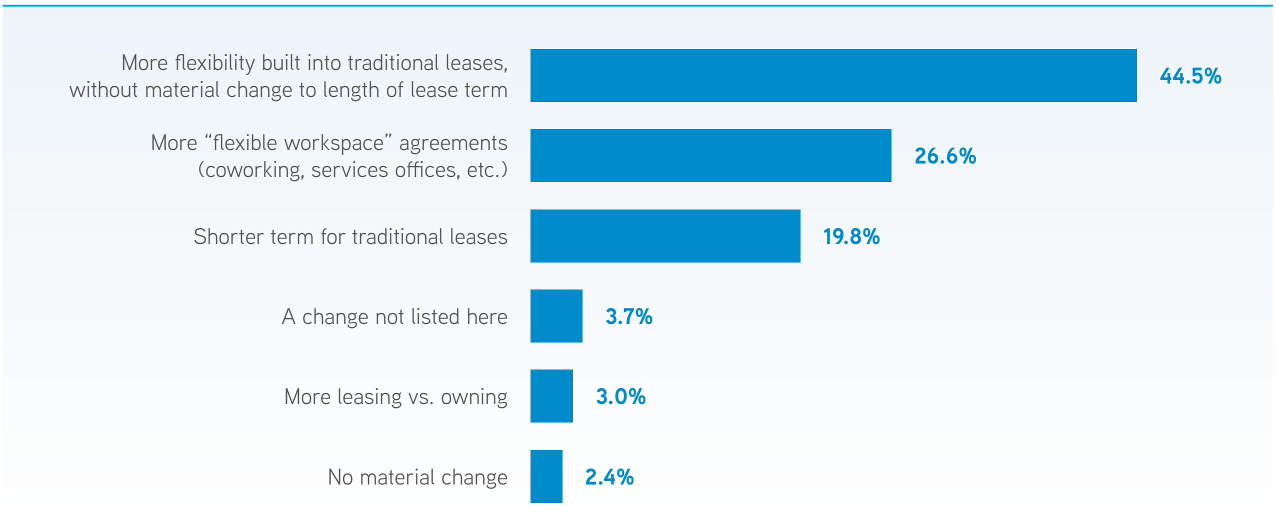
CUSTOMISED, PRIVATE

UTOPICUS | SPAIN

Ultimately, flexible workspace, in any capacity, is the outsourcing of real estate to an operator, whether that operator is the owner of the asset or a third-party flexible workspace operator. While this is typical for start-ups and SMEs, we expect current global market conditions to lead to a large-scale upswing in enterprise outsourcing.

In our recent survey, which reached more than 4,000 occupiers, more than 50% considered a flexible workspace solution to accommodate a longer-term office, which would be considered a core space with stable headcount projections, while almost **half of respondents expected a minimum of 10% of their portfolio to be flexible within three years**. Further cementing this shift, IWG, the world's largest flexible workspace operator, confirmed that it has seen a 35% increase in demand for 50+ desks from Q1 2019 to Q1 2020.

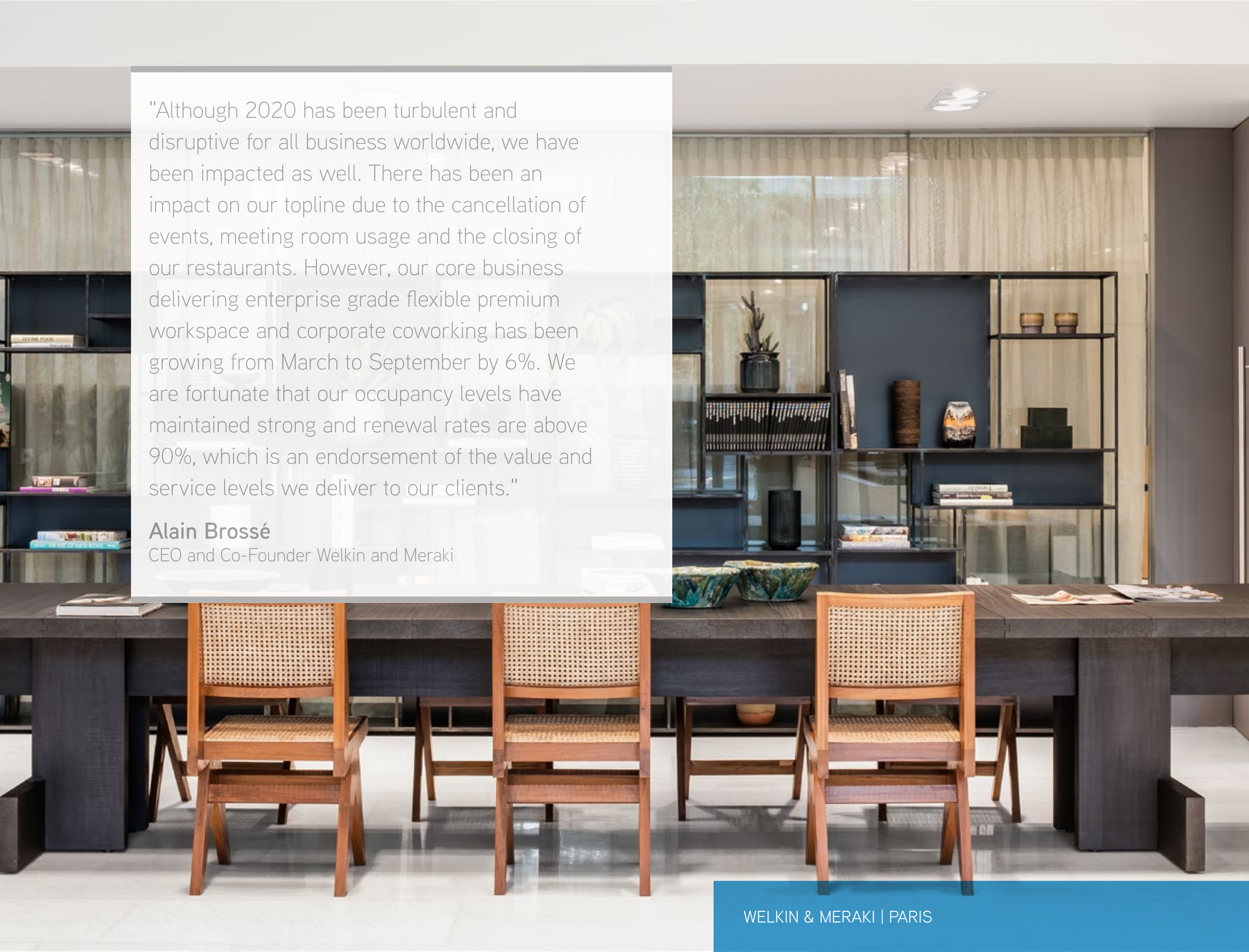
ONE YEAR FROM NOW AND BEYOND, WHAT IS THE MOST SIGNIFICANT CHANGE THAT YOU ENVISION TO COMMON TRANSACTION STRUCTURES?



Source: Work From Home Survey from Colliers Workplace Advisory team

"Although 2020 has been turbulent and disruptive for all business worldwide, we have been impacted as well. There has been an impact on our topline due to the cancellation of events, meeting room usage and the closing of our restaurants. However, our core business delivering enterprise grade flexible premium workspace and corporate coworking has been growing from March to September by 6%. We are fortunate that our occupancy levels have maintained strong and renewal rates are above 90%, which is an endorsement of the value and service levels we deliver to our clients."

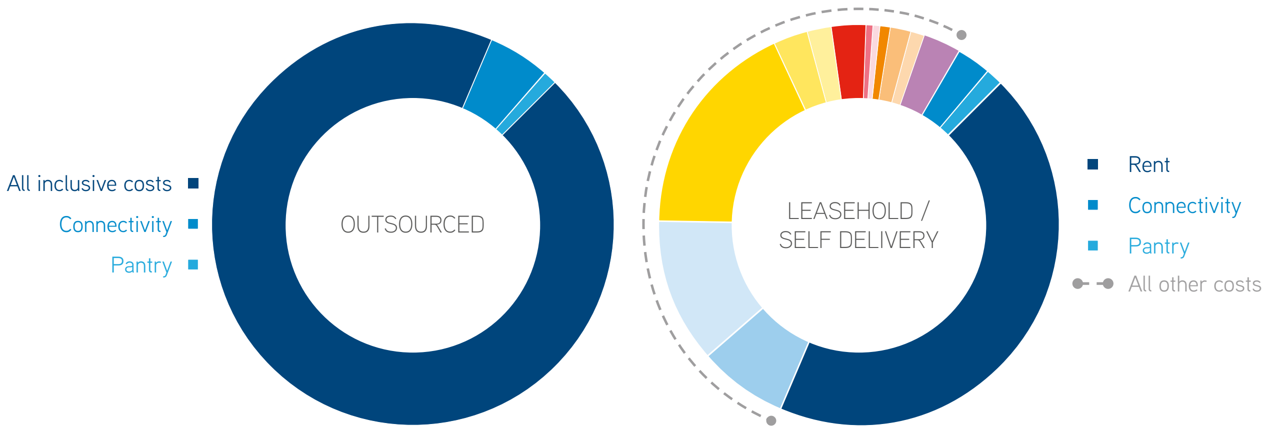
Alain Brossé
CEO and Co-Founder Welkin and Meraki



WELKIN & MERAKI | PARIS

WORKSPACE OUTSOURCING

Outsourcing means an operator delivers all of the elements of the office acquisition and reduces administrative and operational burden of multi-supplier self delivery.



WHAT ARE THE KEY DRIVERS FOR OUTSOURCING TO FLEXIBLE WORKSPACE

AGILITY

When an organisation has unpredictable or dynamic headcount changes, flexible workspace can allow for agility to grow or contract.

FINANCIAL

Outsourcing workspace delivery can reduce capital expenditure and provide operational expense certainty. Reducing long term commitments reduces balance sheet liability and can improve the efficiency of capital.

OPERATIONAL

Outsourcing the delivery of office space can create operational efficiencies. A single supplier is responsible for all workspace operations, this can deliver in-house management and administrative efficiencies.

TRANSFORMATIONAL

Business-driven decisions, expansion into new territories and M&A integrations can all be triggers to use outsourced workspace.

URGENCY

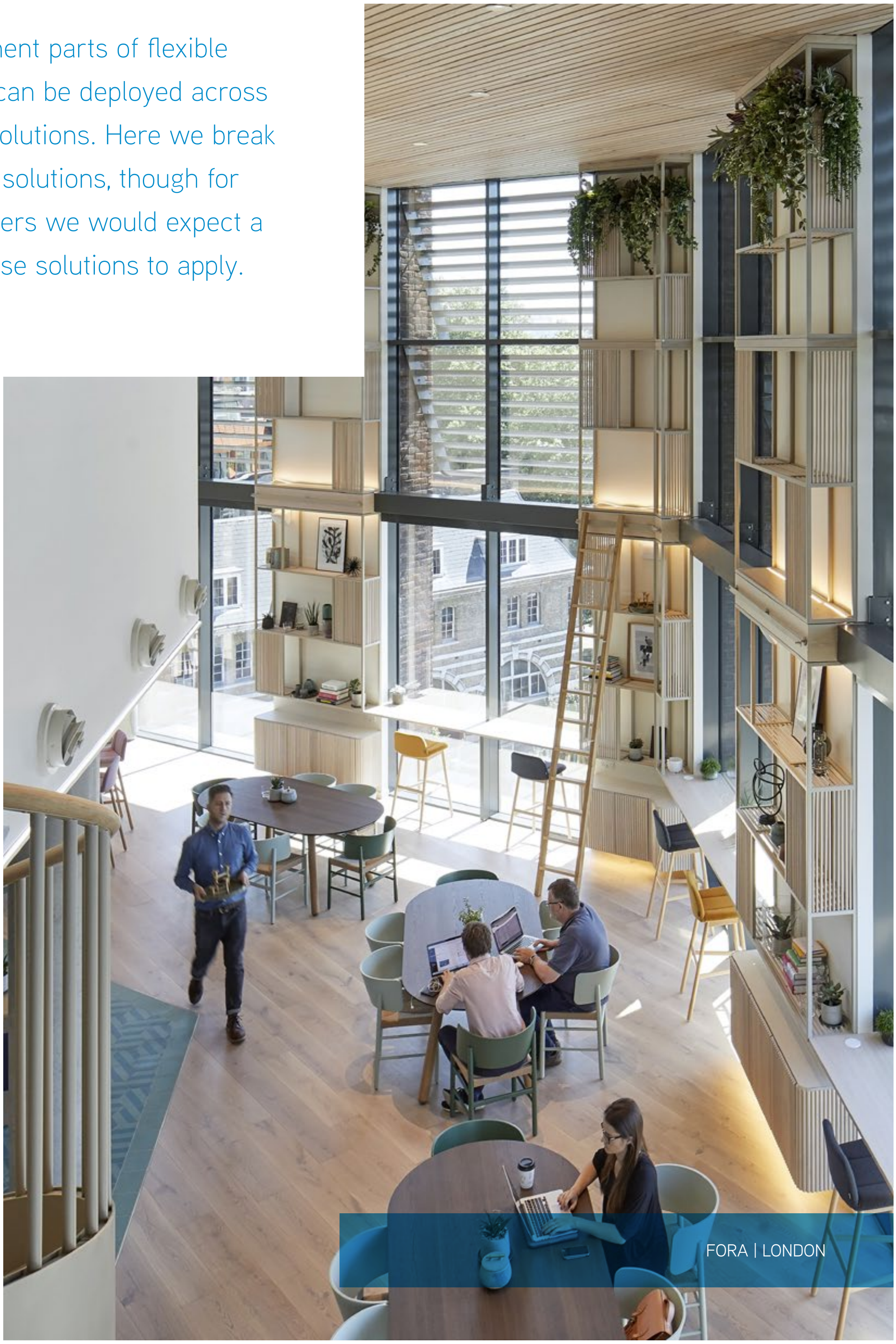
Flexible workspace is usually available on much shorter lead times, existing locations can be occupied immediately and new sites can, at times, be delivered quicker than self delivery due to procurement and supply chain efficiencies.

EMPLOYEE ENGAGEMENT

Operators of flexible workspace typically offer a range of amenities, facilities and services which may be hard to self deliver. This can improve the workplace environment for employees.

STRATEGIC OPTIONS AND DELIVERY MODELS

The component parts of flexible workspace can be deployed across a range of solutions. Here we break down these solutions, though for most occupiers we would expect a range of these solutions to apply.



FORA | LONDON

MANAGED OFFICE

Scenario

- An occupier has a requirement to move a team, division or whole city office, typically 40–300 people.
- The occupier understands the full range of benefits traditional flexible workspace offers but doesn't wish to share all facilities (e.g. pantry and meeting rooms) and wants more ownership and privacy.

Opportunity

- A flexible workspace operator delivers a fully outsourced workspace, which includes all elements of launching and operating an office.
- The new facility is a customised and private environment that looks and feels like the occupier's "own" space, delivered and managed by a third party.
- Occupiers have the ability to increase the flexibility of their portfolio through shorter commitments, mitigate capital expenditure and reduce balance sheet liability.

Considerations

- This type of solution is now being delivered by specialist operators, traditional flexible workspace operators and, in some cases, directly by asset owners.
- Occupiers should be mindful of who is best placed to deliver and operate these environments, especially in new locations.
- Managed space is a grey area that bridges the gap between a lease and traditional flexible workspace, arguably allowing the occupier to have the best of both worlds.

FLEX & CORE

Scenario

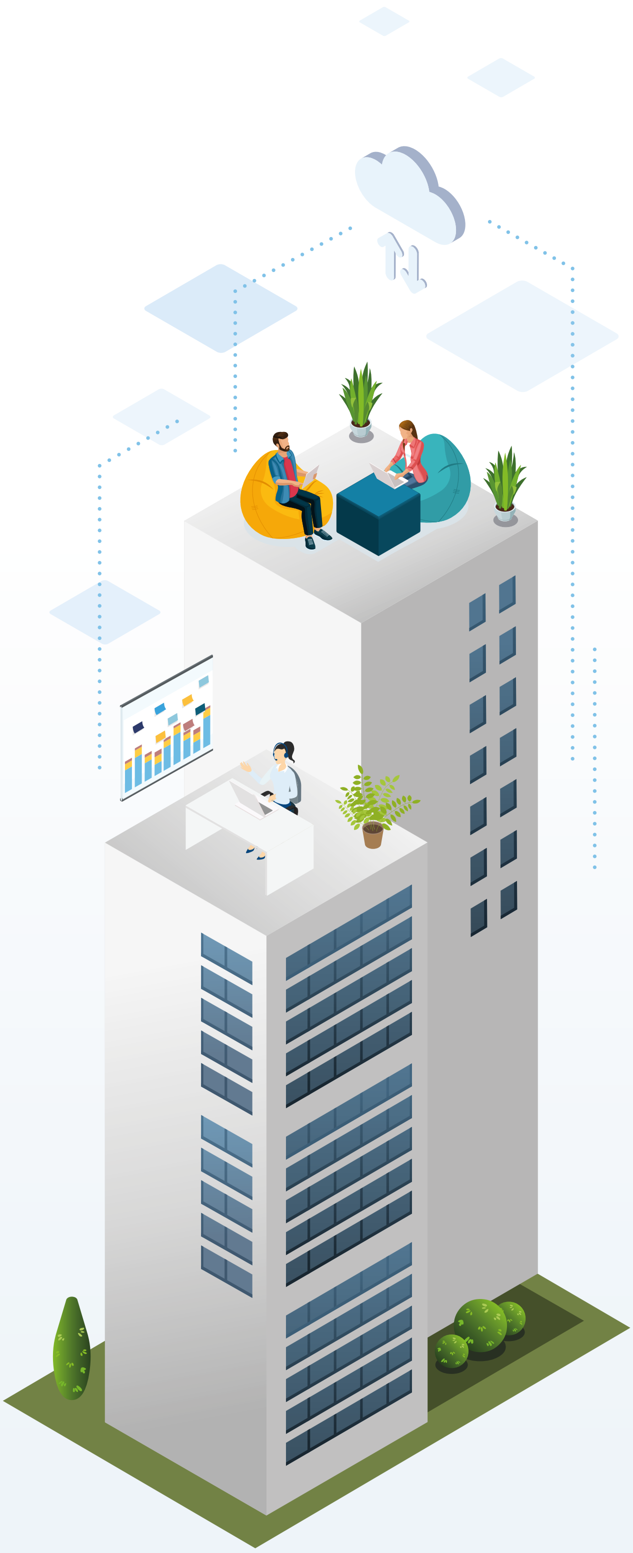
- An occupier has a requirement for new premises with fluctuating and/or unpredictable headcount projections.
- Alternatively, an occupier wishes to outsource some component parts of their real estate, such as meeting space or a project team.

Opportunity

- Identify an operator that will partner to enter an asset.
- Route 1 – The occupier commits to less space for their core requirement and the operator (or asset owner) launches a flexible workspace location in the same building.
- Route 2 – Full operator commitment – the occupier commits to "anchor" the new location and provides options for future expansion.

Considerations

- The occupier has the benefit of long-term security for core operations and flexibility for growth.
- Predetermined expansion options within the flexible workspace demise (this can be whole floors) provide future growth security.
- The occupier has access to amenity spaces such as meeting, conferencing and events spaces, reducing core commitment and elevating the level of amenities.
- Buy in from the asset owner is needed to effectively execute.



REVERSE FLEX

Scenario

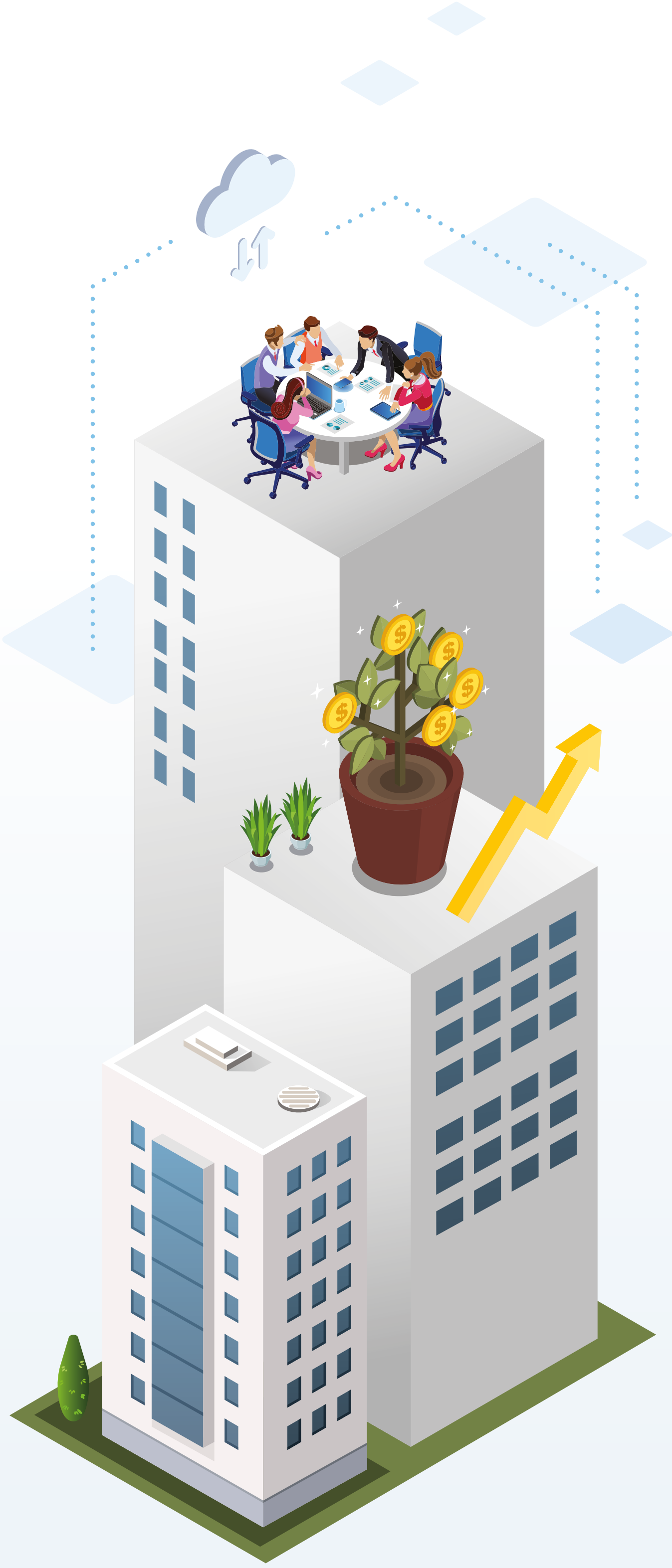
- An occupier has under utilised leasehold space.
- Traditional sub-letting or assignment strategies may not be possible due to market conditions.
- The occupier may want to reoccupy space in the future.

Opportunity

- Reduce property costs by partnering with a flexible workspace operator to repurpose space into flexible workspace.
- Mitigate property expenses and even generate income.
- Operators can use different structures, including; assignment, sublease and management agreements.

Considerations

- Asset owner consent may be required.
- There may be capex required to reconfigure.



HUB & SPOKE

Scenario

- An occupier wants to reduce the reliance on a single headquarter building and implement a dispersed occupancy strategy.

Opportunity

- Reduce real estate costs by shrinking HQ location and taking smaller hubs across a city, region or country. Typically, these would be in lower cost locations.
- Access talent and reduced labour costs in alternative geographical locations.
- Improve work/life balance of employees, reducing commuting times, increased quality of life and reduced living expenses.
- Maintain central flagship HQ, but reduce the amount of space.

Considerations

- Ensuring the consistency of workspace quality across a distributed office portfolio.
- Operational and management considerations of a high number of locations.
- Outsourcing the delivery of these locations can reduce operational burden, improve workspace environment and lower lease liability.

DIGITAL CAMPUS

Scenario

- An occupier has teams or individuals who work remotely or travel frequently. For example, employees who work from clients' offices, on the road, from home or even cafes.

Opportunity

- Membership to a network of drop-in spaces across a region.
- Access to professional workspaces can improve efficiency and productivity for remote workforce.
- Ability to reduce physical office portfolio.
- Reduced fixed property expenses; memberships are highly flexible.

Considerations

- Employees need to have technology that enables them to work remotely.
- There are a variety of local and regional platforms in the market. Colliers has aggregated a range of operators to deliver the Colliers Mobility Pass, the only global platform. Learn more here.

STOREY | LONDON

CONSIDERATIONS FOR ASSET OWNERS

The impact the type of operator agreement has on asset valuation.

The topic of flexible workspace valuation has been of interest to investors, asset owners, operators and debt providers alike, as the effects of COVID-19 have amplified the need for a clear and consistent approach to valuation and as the sector comes under scrutiny. Currently, there is a lack of hard data, a lack of evidence, and a lack of certainty regarding what form of agreement would best fit assets and operators, as well as drive value.

In late 2019, the RICS produced a paper entitled "Valuation of Flexible Workspace," which most in the sector assumed would signpost the methodology and create a standard for the sector. While there is no formal methodology detailed by the RICS, the paper warned of the pitfalls of valuations and advised caution to those without any experience in the sector.

The 'art' of valuation is to seek to replicate the market and reflect the approach a potential investor would adopt when formulating their offer for an asset. Therefore, valuation in this sector should be no different; just as an investor would not look at an asset making strong returns and offer based on the vacant possession value, neither should real estate professionals.

The most common questions we receive from our investor clients relate to the types of agreements in the market and how they impact their valuations, particularly when seeking debt. No conversation on the topic of agreements between asset owner and operator is ever the same. It is true that flexible workspace assets are generally operated using one of four delivery models, but outside of a lease it's rare that we see the exact same deal structure more than once.

We have found that the 'science' of valuation is to reach a consensus between the investors, operators and debt providers in any deal. This is the case in each of the four main bases of value.

THE VANILLA LEASE

The covenant and surety offered by the tenant (operator) is the main factor that will impact valuation. There is generally evidence available; however, we would also factor in the variable nature of that tenant's base of income, i.e. its members and what the strength of their covenant might be.

The three remaining bases should be assessed on the trading potential of the asset.

OWNER OPERATED

The EBITDA of a well-run asset can be comfortably above 200% of the Market Rent of the asset on a vanilla lease basis. While there is limited evidence in the market, in early 2020 the sentiment was that there would be a high volume of M&A activity.

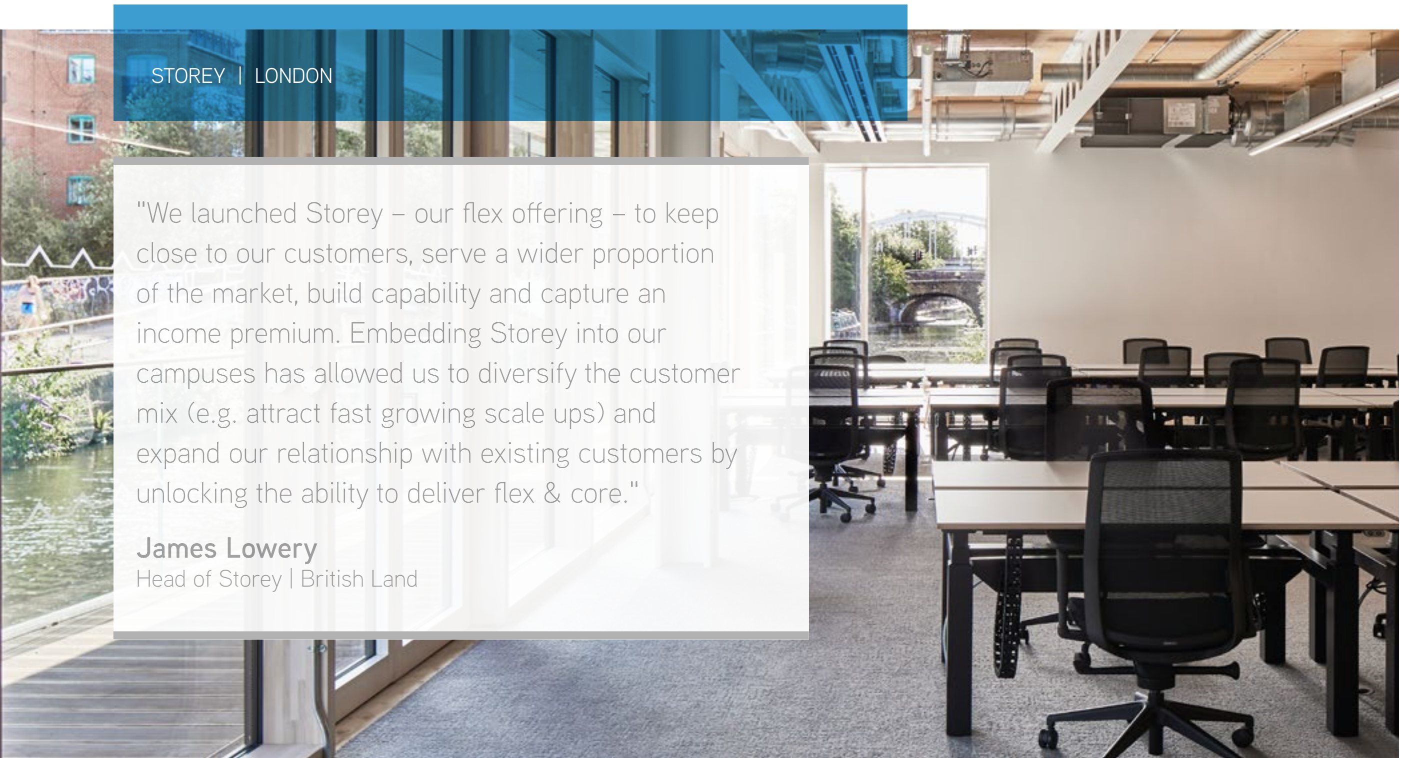
Assets that are owner operated could fundamentally be sold to an alternative operator as a going concern, or to an investor with a view to either self-delivery (which is rare) or inserting the same or an alternative operator on a management agreement.

The Market Rent element of EBITDA is generally 'safe' for a good quality asset that has reached operational maturity. It is the sustainability and future growth potential of the top slice element (the EBITDA over and above the Market Rent) that dictates the yield that should be applied to this element.

HYBRID LEASE

These agreements are becoming more popular. They generally involve a certain level of base rent (let's assume 50% of the Market Rent), with a percentage of turnover/EBITDA element on top. They are considered to provide security to the freeholder on the basis that half of the Market Rent is guaranteed.

This creates another layer to the top-slice method and, again, the yields adopted should reflect the historic trading levels or the trading potential of the asset. A good understanding of how these assets operate is key to determining the appropriate yields, as well as the quality of the asset itself.



STOREY | LONDON

"We launched Storey – our flex offering – to keep close to our customers, serve a wider proportion of the market, build capability and capture an income premium. Embedding Storey into our campuses has allowed us to diversify the customer mix (e.g. attract fast growing scale ups) and expand our relationship with existing customers by unlocking the ability to deliver flex & core."

James Lowery
Head of Storey | British Land

MANAGEMENT AGREEMENTS

These operational agreements offer the least security of income to the freeholder; however, they also offer the greatest potential returns of the non-self-delivered options. Again, valuing these agreements has to be done with regard to the sustainability of the income.

The main issue from a valuation perspective is the real lack of evidence in the market. Where deals have taken place, there has been limited visibility over the actual trading figures, and therefore the returns for the investor.

There is an argument that suggests, from an operational perspective, that management agreements are in fact favourable to a vanilla lease given that some flexible workspace operators have a history of terminating leases prior to natural expiry where the market has moved. This leaves an operational gap that would be less likely to happen under a management agreement.

Finally, some investors see value in having asset management opportunities from having a management agreement rather than a lease.

"For the last twenty years Orega has only worked under management agreement. For our landlord partners, this model means we are solely focused on the performance of their asset and not a quarterly rent demand...we are not just a tenant but an amenity for the building. We have proven this model delivers above market returns and generates value for the asset."

Lynsey O'Keefe
Chief Operating Officer | Orega

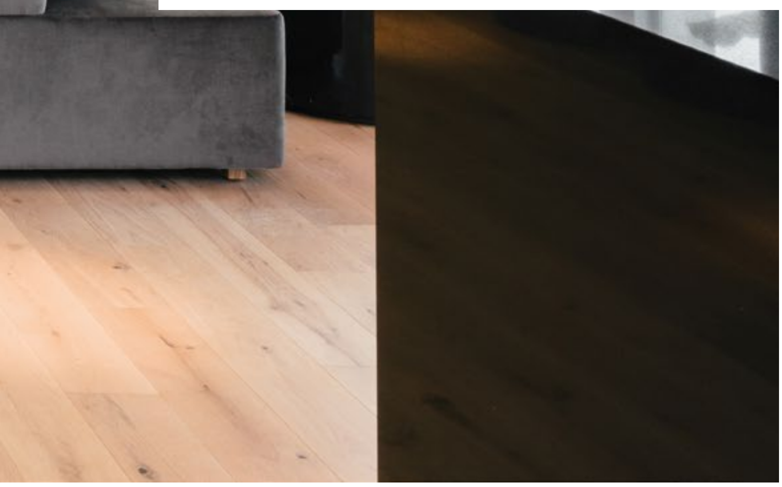
INDUSTRIOUS | NEW YORK

VALUATION ISSUES

There is an element of uncertainty regarding valuation during the period prior to the maturity of the operation for assets on both a Hybrid Lease and Management Agreement. We have found that the concern of many investors is that over this period any valuation for debt purposes will not truly reflect the future potential of the agreement.

In the hospitality sector, the Fair Maintainable Trading (FMT) level is typically adopted. Only with a detailed understanding of the operator's projections and what a FMT can reasonably look like for that particular asset and location, can one reflect the attributes of the agreement in place. This is an agreement that could result in strong returns for the investor, and therefore must be more valuable to an asset owner than having vacant possession.

Another issue surrounds the capex contribution. The investment has to be reflected in the valuation; however, this makes it even more important to demonstrate the future benefit to the asset owner. This can only be the case if the build-out is transferrable and another operator could trade successfully from the premises. Without the ability to assess the trading potential, the impact of the capex on the valuation would make these agreements unviable unless the assets reach maturity on day one, which is unrealistic.



> "Management agreements place the operator on the same side of the table as the asset owner. This enables us to unlock a greater range of solutions for occupiers and a more holistic approach to optimising asset values for the asset owner. It's why Industrious hasn't signed a lease since 2017."
>
> **Jamie Hodari**
> CEO | Industrious

When a hybrid lease or management agreement is in place, an investor is unlikely to view this as held with vacant possession, so why should a valuer? At the same time, an investor is not going to assume that these agreements alone are going to be more valuable (without proof of trading levels) than a vanilla lease. Where the flexible workspace element of an asset is only one part of a multi-let asset, an investor may well see the additional benefits to the rest of the building – this benefit is likely to materialise through a shortening of assumed letting/re-letting periods as well as tenant retention. While any valuer would not be able to quantify this benefit, it provides further weight to the argument that a more positive approach (rather than Vacant Possession) should be adopted.

This again is where the valuer must reflect the approach of an investor. It is then the duty of the valuer to demonstrate this to the debt provider in their report, thereby completing the triangle.

The challenge presented to valuers by the emergence of such a diverse range of deal structures and assets is still significant; however, having an understanding of how mature flexible workspace assets operate and generate income is vital to analysing them as an investment. The Colliers Flex Office Rating System enables us to plot the underlying asset quality and helps determine the potential sustainability of the existing or projected cash flows. While there is limited direct evidence available in the market, it is then up to the valuer to utilise their experience to ensure their adopted approach is one that would be reflected by a purchaser in the market, and considers the risk and returns that are achievable. This is a fundamental principle that is frequently forgotten.

"Copernico offers diversity of product, community management and content delivery through specialised local partners, this means the average length of stay at our centres is higher than that of other international operators. Customers who know the local market usually prefer Copernico, appreciating the flexible solutions and customer experiences more suited to local habits, tastes and needs."

Luca Pasqualotto
CEO and Founder - Copernico

COPERNICO | ITALY

FRAGMENTATION

Over the last five years, supply of flexible workspace in EMEA has grown exponentially, up nearly three fold on 2011-15. In many markets across the region WeWork were responsible for much of this growth. However, that is not the full story. The EMEA flexible office market is highly fragmented with over 3,300 different locations operated by 1,300 different operators.

There are many excellent local operators who do not have plans for world domination, rather focusing on delivering best in class service in a single city or country. Their ability to adapt their offer to the local market practices is often a key point of difference and many occupiers want this “local touch”.

Recent events have caused many operators including WeWork to re-evaluate their portfolio and pipeline and this has led to some locations closing or not ever opening. There is already tremendous choice and we expect to see the market continue to grow in 2021 as new operators enter the market, existing operators look to expand, using more sustainable models and asset owners develop their own products.

EMEA has such diversity of flexible workspace and operators who embrace the local market nuances, they will be able to capture occupier demand which is looking for best in class flexible workspace.

COMMUNITY IN A POST-COVID-19 WORLD

The various levels of lockdown around the world have restricted access to the office and have consequently limited social interaction. Social relationships are a major contributor to employee wellbeing. Prior to COVID-19, most employees' social interactions were with colleagues, either in organised or informal after-work settings. Without the social elements of work, the opportunities to collaborate, innovate and learn are also limited.

In a post-COVID-19 world, it is critical for flexible workspace operators to cultivate community by promoting wellness programs and thoughtful learning opportunities, and to foster a collaborative environment that encourages connection. We forecast that occupiers will seek out operators that can deliver holistic offerings and manage their employees in a safe environment, and that this will be a driver for greater levels of enterprise outsourcing.

"A sense of belonging has never been more important to people than it is right now.

The seismic shift caused by the global pandemic has created a unique collective experience, and now more than ever, people are joining together and seeking unity, in whichever way they can.

Working from home has changed the landscape, but there is an innate desire within us all to feel connected. PLATF9RM reflects this; we give people a place to anchor themselves, to be a part of something inspiring and offer a work near home option."

Seb Royle
Founder & CEO - PLATF9RM

HOVE TOWN HALL | BRIGHTON

FLEXIBLE WORKSPACE CONSULTING

Colliers International's global flexible workspace consulting team works with all stakeholders in the sector. Our team of in-house experts delivers strategic advisory to operators, develops asset owners' flexible workspace approaches, and unlocks opportunities with creative solutions for our occupier clients.

Our integrated approach provides us with a holistic perspective on the sector and our clients benefit from the team's unparalleled track record and experience. Acting exclusively as an advisor, with no competing product, our independent market positioning allows us to provide uncompromised outcomes for our operator, asset owner and occupier clients.

OPERATOR

- Market Growth Strategy
- New Location Acquisition
- M&A
- Fundraising

OCCUPIER

- Strategic Advisory
- Portfolio Diagnostics
- Transaction Management
- Creative Deal Structuring

ASSET OWNER

- Strategic Advisory
- Creative Positioning
- Transaction Management
- Feasibility and Valuation

ABOUT COLLIERS INTERNATIONAL

Colliers International (NASDAQ, TSX: CIGI) is a leading real estate professional services and investment management company. With operations in 68 countries, our more than 15,000 enterprising professionals work collaboratively to provide expert advice to maximize the value of property for real estate occupiers, owners and investors. For more than 25 years, our experienced leadership, owning approximately 40% of our equity, has delivered compound annual investment returns of almost 20% for shareholders. In 2019, corporate revenues were more than $3.0 billion ($3.5 billion including affiliates), with $33 billion of assets under management in our investment management segment. Learn more about how we accelerate success at corporate.colliers.com, Twitter@Colliers or LinkedIn.

OUR GLOBAL FLEXIBLE WORKSPACE EXPERTS & REPORT CONTRIBUTORS

TOM SLEIGH

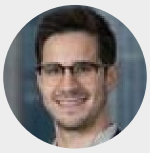
Head of Flexible Workspace Consulting | EMEA
+44 7738 004095
tom.sleigh@colliers.com

HARRY FLOOD

Director | Valuations & Advisory Services | EMEA
+44 7917 584467
harry.flood@colliers.com

JONATHAN WRIGHT

Director | Flexible Workspace Consulting | Asia
+852 9020 9200
jonathan.wright@colliers.com



FRANCESCO DE CAMILLI

Vice President | Flexible Workspace Consulting | Americas
+1 2039277283
francesco.dexamilli@colliers.com

SAMI SCHIAVI

Manager | Flexible Workspace Specialist | Australia
+61 427 593 280
sami.schiavi@colliers.com

RESEARCH & REPORT CONTRIBUTORS

DAMIAN HARRINGTON
Head of Research | EMEA
+44 7867 360489
damian.harrington@colliers.com

ISTVAN TOTH
Associate Director | Research | EMEA
+44 7566 292579
istvan.toth@colliers.com

RAKESH KUNHIRAMAN
Senior Director | Research | Asia
+65 9771 5721
rakesh.kunhiraman@colliers.com

EMEA OCCUPIER SERVICES PLATFORM LEADERS

ANDREW HALLISSEY
Executive Managing Director
Occupier Services
+44 7483 928961
andrew.hallissey@colliers.com

SAM ADDISON
Head of Project Management
+44 7592 116151
sam.addison@colliers.com

JANJAAP BOOGAARD
Head of Workplace Advisory
+44 7544 163808
janjaap.boogaard@colliers.com

MAXINE BURNETT
Head of Lease Administration
+44 7706 001102
maxine.burnett@colliers.com

ROBERT CAMPKIN
Head of Corporate Capital Solutions
+44 7845 051068
robert.campkin@colliers.com

WILL HARRIS
Head of Technology and Innovation
+44 7717 738529
william.harris@colliers.com

PETER LEYBURN
Head of Cross Border Tenant Representation
+44 7785 115108
peter.leyburn@colliers.com

JAMES RAWDON-MOGG
Head of Enterprise Solutions
+44 7880 023032
james.rawdon-mogg@colliers.com