



Judy Jang

Associate Director | Research | Korea

+822 6325 1918

[judy.jang@colliers.com](mailto:judy.jang@colliers.com)

# FLEXIBLE WORKSPACE MARKET AFTER COVID-19

## Insight & Recommendations

COVID-19 has led occupier, asset owners, and investors to prepare for significant changes in the flexible workspace sector.

- > Occupiers are advised to leverage opportunities to negotiate discounts on membership fees for flexible workspace as market demand softens.
- > Asset owners should consider how flexible workspace adds value to their portfolios, while realizing flexible workspaces are no longer a quick solution to fill vacancies. Deals should focus on well capitalized operators and be structured to increase the provision of amenities and services.
- > Flexible workspace operators need to consider business models that can minimize vacancy risks through win-win relationships with asset owners.

## 150 flexible workspace locations



There are about 150 flexible workspace locations in Seoul, with 46 of them in Grade A buildings.

We estimate 77 of these locations are operated by multi-location operators.

## 24 flexible workspace operators



There are about 24 flexible workspace operators in Seoul, these include IWG, WeWork, JustCo, The Executive Centre and domestic operators; Fast Five and Spark Plus.

## KRW400,000 : (USD326) Average monthly Desk Cost



The desk rate for private offices varies widely, but the average is about KRW400,000 (USD326) per month.

## 50% of locations are in the Gangnam area



Among 150 flexible workspace locations in Seoul, more than 50% of them are located in the Gangnam area. Within the three major submarkets, over two-thirds of flexible workspace locations are in Gangnam.

With global flexible workspace operators expanding in Korea and policies supporting demand from startups, the past three years were a boom period for flexible workspace operator growth. However, following the COVID-19 outbreak, we expect to see changes in the market, including changes to the size of the market and changes to operating strategies. In addition, we also believe that the smaller operators who emerged during the peak growth period are likely to be forced to exit, unless they have a robust platform or specific niche. Until COVID-19 subsides, we expect the growth of flexible workspace operators to be largely paused.

Meanwhile, as the pandemic creates a challenging economic reality and makes the business environment more uncertain occupiers are likely to revisit their occupancy models to integrate a greater level of flexible workspace in the long term, which should boost occupancy levels across the sector.

## Major flexible workspace operators

Major flexible workspace operators that have locations in Grade A and B buildings in Seoul's key sub-markets include global operators IWG, WeWork, JustCo, and TEC, as well as Korean companies such as Fast Five and Spark Plus.

Flexible workspace operators that expanded aggressively into new locations in the past have slowed their expansion due to COVID-19 and are beginning to cut desk rates.

According to Chosun Biz News, WeWork has requested a three-month rent reprieve from landlords, while JustCo announced it would offer their occupiers some concessions in May.

COVID-19 has contributed to a pause in expansion for global operators, with the exception of IWG who are likely to continue growth due to their recent share offering. Meanwhile, we expect Korean operators, specifically, Fast Five and Spark Plus to continue opening new locations. In May, Fast Five had the No. 1 market position in Korea based on number of locations and plans to go public this year. Spark Plus also continues to actively expand, and recently opened a new location in Gangnam, their 13<sup>th</sup> in total.

### Major flexible workspace operators

Company Name	Number
Fast Five	25
WeWork	20
Regus Korea	13
Spark Plus	13
JustCo	5
The Executive Center	5

Source: Colliers International, May. 2020



## Work environment changes caused by COVID-19

Due to COVID-19, large occupiers have dispersed their employees across different offices. For example, SK Telecom analyzed where employees live and allocated them to "base offices" within a 20-minute commute from their homes. SK Telecom is planning to roll out a hub and spoke model that allows employees to choose among 10 base offices. SK Innovation has been operating a *1 week work, 3 week home work* system for some departments.

NHN adopted telecommuting on a long-term basis after their initial telecommuting period ended. They have adopted a remote work system that allows employees to choose to work from home one day per week.

Going forward, expansion of manpower may no longer require expansion of office space. We may see an adjustment in strategies for space utilization with a focus on more efficient utilization of workspace.

Companies with a large number of employees may need to consider rent as a variable cost, rather than a fixed cost, as rent may fluctuate depending on the organization's occupancy model. We expect an increase in demand for flexible workspace locations as COVID-19 triggers more widespread adoption of distributed working environments, including telecommuting.

## Changes in needs of flexible workspace tenants

Going forward, we expect demand for flexible workspace to come from occupiers seeking cost-reduction, rather than demand from startups or in-house expansion.

We expect demand for flexible workspace to rise as they become a useful tool to assist with worker redistribution and social distancing strategies designed to slow the spread of COVID-19.

As COVID-19 has increased uncertainty in the global economy, we expect it to trigger more cost-reduction measures, including office fit-out cost reduction. At the same time, we see an increase in the needs of contingency plan to respond more flexibly to abrupt, economic challenges.



## Changes in services provided

Flexible workspace operators have emphasized the sharing and network aspects of flexible workspace. This may change into to an emphasis on providing services focused on independence and security. We expect flexible workspace demand to be strengthened by the need for cost savings and flexible organization of large and medium-sized companies. The number of flexible workspace operators specialized by industry such as legal, finance, and fashion can also increase.

## Growing need for new flexible workspace strategies

We expect flexible workspace operators to pivot their growth strategies to mitigate the exposure to the risks of the real estate economy and vacancy due to the Covid-19. We expect deeper partnerships between asset owners and operators to emerge in the form of management agreements and partnerships, while some asset owners may choose to develop their own concepts.

An alternative model, which helps to mitigate risk, is for the operator to sign a partnership agreement with the landlord, instead of leasing and operating buildings directly. The landlord builds out and pays for the flexible workspace, and the operator oversees the running as well as the marketing and leasing of the space, with rental income split between them.

Colliers offers Flexible Workspace Consulting is a global service providing advisory, consulting and transaction services to operator, occupiers and asset owners.

Operators can benefit from new market mapping; occupiers can benefit from an analysis of their portfolio and asset owners can benefit from asset repositioning and deal structure advice. All our clients can benefit from our strategic advisory and transaction management services.

## New 'sharing economy' business models

Just as the flexible workspace sector has expanded for the past few years, investors need to pay attention to another shared platform service, the shared kitchen. In line with growing demand for food delivery due to COVID-19, shared kitchen operators have received a rising number of lease inquiries.

In addition, shared housing is emerging as another sharing economy trend. The residential sector has not been a major investment target for institutional investors, but stable cash flow and operating returns are leading investors to consider shared housing as a new investment target. For example, IGIS Asset Management recently set up a public housing blind fund of about KRW250 billion (USD205 million).

In addition, shared logistics that use idle space in metropolitan areas are emerging as a new sharing economy trend. In the long-term, this means that not only can we expect flexible workspace demand rise, but also other concepts such as shared housing and shared logistics are likely to gain further traction.



We recommend investors to monitor both shared offices and other shared economy business models such as shared kitchens, shared housing, and shared logistics. Commercial real estate investors also need to continue to be interested in the shared economy business model in order to secure a return on building operations.

Therefore, we advise real estate investors to explore new opportunities in commercial real estate sectors and operational models that are set to emerge after the COVID-19 epidemic stabilizes.

## Primary Author:

### Judy Jang

Associate Director | Research | Korea

+82 2 6325 1918

[judy.jang@colliers.com](mailto:judy.jang@colliers.com)

## For further information, please contact:

### Robert Wilkinson

Managing Director | Korea

+82 2 6325 1901

[Robert.Wilkinson@colliers.com](mailto:Robert.Wilkinson@colliers.com)

### Andrew Haskins

Executive Director | Research | Asia

+852 2822 0511

[andrew.haskins@colliers.com](mailto:andrew.haskins@colliers.com)

### Joon Lee

Senior Director | CMIS | Korea

+82 2 6325 1907

[joon.lee@colliers.com](mailto:joon.lee@colliers.com)

### Jay Cho

Director | Office Services | Korea

+82 2 6325 1905

[jay.cho@colliers.com](mailto:jay.cho@colliers.com)

### Jonathan Wright

Director | Flexible Workspace Consulting | Asia

+852 9020 9200

[Jonathan.Wright@colliers.com](mailto:Jonathan.Wright@colliers.com)

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