Flexible Workspace – Here To Stay
Globally and in Asia, demand for flexible workspace is rising. Over 2016 we expect flexible working operators to lease 20% more office space in Hong Kong than Chinese groups took up in 2015; and they are expanding in Shanghai too. Landlords can expect higher demand for space, but must build relations with a new type of tenant. As occupiers, international flexible working operators should be competitive in Hong Kong and Singapore, but will find it tough to penetrate China. Landlords and investors alike should pay heed to flexible working operators’ business plans, since over-expansion is a risk.

Globally and in Asia, the key factors driving demand for flexible workspace are: 1) the arrival of a new generation of workers, 2) increased attention to technology and innovation, and 3) the rise of flexible working operators offering serviced offices and coworking space. In Asia, growth in fintech and internet applications is reinforcing these trends. Flexible workspace looks set to stay.

The new trend is already making its presence felt. Over 2016 we expect flexible working operators to lease 20% more office space in Hong Kong than Chinese groups took up in 2015 – and Chinese demand has supported rents. Benefiting from state support, Singapore is becoming a business start-up launch pad for Southeast Asia, and there are now over 40 flexible working centres in the city. We see solid demand for flexible workspace in China, where Beijing is a hub for innovation. While China has established local flexible working operators, the market is also a target for international groups like WeWork, which has leased two-thirds more space in Shanghai so far in 2016 than in Hong Kong.

The spread of flexible working space has implications for all property market players. Flexible working operators are boosting demand, so over time landlords may expect greater competition for office space. Moreover, flexible working operators taking up ample space will benefit developers with high vacancy rates or with buildings under construction hoping to pre-let. However, if a flexible working space operator’s clients do not fit with a landlord’s existing tenant mix, problems may ensue.

We advise smaller flexible working occupiers in Hong Kong and Singapore to look for space in the CBD fringe or in non-central areas. International flexible working operators should prove competitive in these markets. By contrast, we expect that international groups will find it tough to penetrate the Beijing and Shanghai markets where the local players have high market shares.

Investors should pay heed to flexible working operators’ business plans, and ensure their cash flows are adequate to cover rent and capex needs. We see a risk of over-expansion on a local scale by flexible working space operators, which raises the possibility of a glut of empty space appearing in certain areas, depressing rents and maybe capital values. This risk applies particularly to flexible working space operators focusing on the low end of the market, and less so to companies occupying high-grade buildings in prime locations.

### Graph: Occupation of HK office space by Chinese groups in 2015 and flexible working operators in 2016

- **Mainland Chinese tenants in 2015**: 400,000 (1.1%)
- **Flexible working operators in 2016 (estimated)**: 475,000 (1.3%)

Source: Colliers’ estimates
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Three factors drive desire for flexible working space

Globally and in Asia, various factors are driving increased demand for more flexible and engaging working space. In our opinion, the most important factors are: 1) the appearance in the workforce of a new and younger generation, 2) increasing awareness of technology and the importance of innovation, and 3) the emergence in property markets of coworking operating companies which are complementing the role of traditional serviced office operators. Since the boundary between serviced office operators and coworking space operators has become rather blurred, we think that it is easiest to group the two categories together under the heading of flexible working space operators.

The new generation of workers

The new generation of workers is often called the millennial generation, referring to people born in the run-up to the start of the 21st Century. Especially in more developed markets, “millennials” have a reputation for blending work and personal time. We have calculated the proportion of the Asian working population by age group using United Nations estimates for 2015, 2020, 2025 and 2030 (see table below). On this basis millennials currently represent 47% of the aggregate Asian workforce. This proportion is boosted by the fact that there are eight large emerging Asian markets (countries such as India, Pakistan and Vietnam) in which at least 49% of the population is aged below 30, and is not truly representative of more advanced markets such as China, Hong Kong and Japan, where the proportion of the population aged below 30 ranges between 40% and 28%. Nevertheless, as a rough indication of the extent to which millennials are already a powerful force in Asian economies, the 47% figure is helpful.

<table>
<thead>
<tr>
<th>Generation</th>
<th>Born year</th>
<th>Age in 2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Baby Boomers</td>
<td>1946-1964</td>
<td>52-70</td>
</tr>
<tr>
<td>Gen X</td>
<td>1965-1980</td>
<td>36-51</td>
</tr>
<tr>
<td>Next Gen</td>
<td>From 2001</td>
<td>0-16</td>
</tr>
</tbody>
</table>

Note: There are no formally agreed time periods for generations; the above ranges are based on various definitions quoted in Wikipedia.

As the table indicates, millennials will dominate the total Asian workforce for the next several years. The post-millennial “Next Gen” should account for 12% of the Asian working population by 2020. Conversely, by 2030, the “Baby Boomer” generation born in the aftermath of World War Two will have entirely exited the Asian working population, with a large portion of the subsequent Gen X workforce also fading from the scene.

What kind of environment do millennials in the more advanced Asian markets want to work in? We would argue that millennial-friendly workplace design is based on three key amenities: collaborative space, relaxation rooms, and provision of food and drink. Provision of these amenities in traditional Asian office environments is limited, partly due to general lack of space in crowded city centres, and partly for cultural reasons. Specially designed coworking office buildings help create an environment much more conducive to the desires and aspirations of the younger millennial workforce.

Increasing awareness of technology and the importance of innovation

Technological advancement creates opportunities for new businesses and start-ups. The emerging fintech (financial technology) sector and the Internet of Things, standing for the network of objects embedded with electronics, software and sensors, have become key growth areas within economically important Asian centres. As we discuss in greater detail in the appendix to this report, large banks and financial groups are increasingly trying to adopt fintech solutions in order both to rationalise their operations and to defend themselves against new challenges.
Many of these solutions are being developed by finance professionals with long experience who have found that the bureaucratic organisation of traditional large financial groups hampers innovation, and so prefer to work either in new “incubator” offices being opened by banks outside their headquarters operations or in more flexible, entrepreneurial environments such as coworking centres.

In the same way, as we also mention in the appendix, the top three areas for start-up businesses in Hong Kong are related to the Internet of Things. Entrepreneurs in these areas accounted for 43% of total entrepreneurs in Hong Kong in 2015, according to StartmeupHK, a web portal which provides information and assistance to start-up operations. Similarly, in Singapore, technology start-ups dominate new business launches: the Singapore government’s trade support agency SPRING estimates that Singapore-based start-up ventures working on technologies grew from 2,800 firms in 2004 to 5,400 firms in 2014.

China’s technology sector has grown rapidly in recent years, and the serviced office and flexible working sector has grown in tandem in order to satisfy the demand for flexible space. Local governments in Shanghai, Beijing and other cities have been moving to launch venture funds for university graduates and professionals, subsidising rent and tax payments for the start-ups. Despite the fact that Shanghai ranks first among Chinese cities by GDP and is the nation’s leading financial centre, Beijing hosts the majority of China’s start-up businesses, possibly because Shanghai is more focused on the financial and retail sectors and less focused on the technology field. This situation is borne out by the results of a survey by National Survey Research Center at Renmin University of China and its partners on 1 March 2016(1), which interviewed 2,100 entrepreneurs across 21 cities in China and suggested that Beijing has the best start-up environment in China.

It is not surprising, therefore, that Beijing should have become a centre for new and more flexible modes of working. Lying at the heart of technological innovation in China today is Zhongguancun, the area in Beijing’s Haidian District which is China’s equivalent of Silicon Valley. Zhongguancun is home to more than 40 universities including Peking University, Tsinghua University and Renmin University of China, as well as a large number of technology companies. Fuelled by a substantial increase in venture capital deals and continuing high activity by leading internet groups such as Alibaba, Tencent, Baidu and Sina, major serviced office and flexible working space operators have clustered in this area to satisfy demand for office space.

Emergence of flexible working space operators

Serviced offices are a well-known concept. A serviced office operator such as Regus of Luxembourg leases a building from a landlord, fits it out with desks and IT equipment and then rents out space within the building. The end-user, typically a company looking for temporary or supplemental space, obtains a private office area within the building and undertakes its business within the confines of that space.

A newer concept, true coworking space is essentially open-plan office accommodation. A coworking space operator leases a building from a landlord, fits it out with desks and IT equipment, and then rents out space to end-users on a desk by desk basis. The operator seeks to promote collaboration and integration of these users, or “members” as they are often known, in order to foster a community.

The companies that have risen to prominence in this field, for example, WeWork and NeueHouse of the US, harness both approaches: they offer serviced offices and coworking space within the same location. In consequence, the end-user has the choice of either solution. Besides this flexibility, end-users benefit from a sophisticated online platform, community events and appealing interior design.

As the above discussion should have made clear, the domains of traditional serviced office operators and coworking operators are increasingly converging. In our view, this means that it no longer makes sense to insist on a rigid distinction between the two. This is why we have grouped together serviced office and coworking space companies under the heading of “flexible working operators”, even if that term is not yet well-established.

Nor would it be correct to assume that flexible working operators provide a working environment which is necessarily inferior to that provided in traditional office space. On the contrary, certain flexible working companies, notably Servcorp of Australia pride themselves on only leasing space in prime buildings. In Hong Kong, for example, Servcorp occupies 22,000 square feet of space in Two IFC, the most prestigious building in the territory.

North America and Europe are the two regions where flexible working or coworking is most established. According to First Results of The Global Coworking Survey 2015-16 by the online coworking space magazine Deskmag(2), the number of coworking centres (to use what seems to be the standard industry term, although “spaces” or “sites” might be just as good) worldwide rose from 3,400 in October 2013 to 7,800 in October 2015, representing growth of 129% in two
Major flexible working space operators with presence in Asia

<table>
<thead>
<tr>
<th>Company name</th>
<th>Domicile</th>
<th>Ownership</th>
<th>Market valuation (USD billion)</th>
<th>Office space (million sq m)</th>
<th>Office space (million sq ft)</th>
</tr>
</thead>
<tbody>
<tr>
<td>WeWork</td>
<td>US</td>
<td>Private</td>
<td>16.0-17.0(1)</td>
<td>0.46</td>
<td>5.0</td>
</tr>
<tr>
<td>Servcorp</td>
<td>Australia</td>
<td>Public</td>
<td>0.5(2)</td>
<td>0.25</td>
<td>2.7(2)</td>
</tr>
<tr>
<td>Regus</td>
<td>Luxembourg</td>
<td>Public</td>
<td>4.2</td>
<td>4.27</td>
<td>66.0</td>
</tr>
<tr>
<td>SOHO 3Q</td>
<td>China</td>
<td>Private</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>Compass Offices</td>
<td>Hong Kong</td>
<td>Private</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>The Executive Centre</td>
<td>Hong Kong</td>
<td>Private</td>
<td>0.14</td>
<td>Over 1.5(5)</td>
<td></td>
</tr>
</tbody>
</table>

Source: SOHO China annual report 2015; Bloomberg; Wall Street Journal; Regus annual report 2015
Notes:
(2) Market capitalisation at 2 June 2016
(3) Average size of approximate 18,000 sq ft per office floor for 150 floors, according to Servcorp’s staff
(4) SOHO 3Q’s parent SOHO China is listed, with a market capitalisation of USD2.4 billion. SOHO China owns total floor space of 0.16 million square metres or 1.7 million square feet in Beijing and Shanghai. As at September 2014

years. In February 2016, another survey by Deskmag, Final Results Of The Global Coworking Survey 2016(3), showed that 56% of coworking space operators had an intention to expand to more locations in Asia, compared to the global result of 36% of operators wishing to expand.

(3) See http://www.slideshare.net/carstenfoertsch/1st-results-of-the-global-coworking-survey-201516

Incidentally, the first survey just cited also showed that commercial buildings are preferred as coworking space sites. The survey suggested that 51% of coworking space sites globally were located in commercial buildings, compared to 20% in industrial buildings despite the lower rental cost of the latter.

The best-known flexible working space operator globally is probably WeWork. Founded in 2010 in the US, this is a private company which has expanded to at least 80 locations in nearly 30 cities around the world. The Wall Street Journal has reported that WeWork had more than 5 million square feet open in 10 March 2016, and it has leased so much space in its home market that it has become the biggest occupier of space in New York’s Manhattan. In Asia WeWork is already present in Shanghai and Hong Kong and has ample capability to expand further, considering that progressive rounds of financing by new private equity investors have given the company an imputed valuation of USD16.0-17.0 billion. While certain observers consider WeWork’s very high imputed valuation to be evidence of a bubble in the flexible working space market, we should note that the private equity investors in the company such large and well-known groups as Fidelity Investments, T. Rowe Price, Wellington Management and Goldman Sachs.

Looking at other major flexible working space operators, in terms of total floor space under management, Regus is the world’s largest provider of flexible working space by far. With headquarters in Luxembourg but listed in the UK on the London Stock Exchange, Regus runs over 46 million square feet (4.3 million square metres) of space in 2,768 locations across 106 countries, according to its annual report in 2015. The company’s original focus was serviced offices, and this is still the business for which the company is best-known. However, Regus provides a wide range of additional services including virtual offices and coworking space. Regus’ market capitalisation currently stands at USD4.2 billion.

Compass Offices is a private company based in Hong Kong which has 23 locations in the city. Founded in 2009, this provider of serviced and virtual offices has expanded into 40 locations in seven Asian countries.

The Executive Centre, another Hong Kong-based private company, had total office space under management of 1.5 million square feet (0.14 million square metres) as of September 2015, spread across more than 70 centres in Hong Kong, mainland China, Macau, Taiwan, India, Indonesia, Japan, South Korea, Singapore and Australia. It is worth noting that the Executive Centre launched its first coworking space in Singapore at Marina Bay Finance Centre Tower 1 and is now present at four locations across the city, including additionally Ocean Financial Centre, One Raffles Quay and Six Battery Road.

Founded in Sydney in 1978, the Australian company Servcorp currently occupies 2.7 million square feet (0.25 million square metres) of office space, which it uses to offer executive suite, virtual office and coworking space. The company has expanded to 52 cities globally including 17 urban centres in Asia. Servcorp is listed with a market capitalisation of AUD0.7 billion (USD0.5 billion).

SOHO China is a real estate developer founded in 1995; it has a focus on office property in Beijing and
Shanghai. SOHO China is listed in Hong Kong with a market capitalisation of RMB15.3 billion (USD2.4bn). The company launched a shared office solution called SOHO 3Q in February 2015 in its 12 modern office buildings. SOHO 3Q is offering over 10,000 desks to 30,000 members, making the business one of the largest flexible working space operators in China.

Increased willingness by companies to use flexible working space

As the concept of flexible working space has moved steadily into the commercial mainstream, so larger companies, including multinational corporations (MNCs), have become more willing to accept it. This is partly because flexible working space offers large companies an alternative to committing themselves to binding leases – an option which is especially attractive in times of economic difficulty. Another reason is that a number of flexible working operators have been moving up-market by securing space in prime buildings or prime locations.

In consequence, in our view the idea that serviced offices necessarily house small companies, and that coworking spaces are the realm only of small-scale or casual entrepreneurs, is increasingly out-of-date. To provide some simple examples, we estimate that MNCs represent over one-half of Servcorp’s global client base. To give two concrete examples, the large investment firm ADIA of the United Arab Emirates is a client of Servcorp in Hong Kong, while the Qatar office of UBS of Switzerland is housed in a Servcorp building. In the same way, WeWork houses the New York office of the UK’s Guardian newspaper.

Flexible working space: surge in supply and demand

Hong Kong

The new flexible working operators have already made greater inroads into Asian markets than is generally appreciated. Much attention has been devoted to the impact on the Hong Kong office property market of the recent strong demand for office space, especially in the core Central district, from mainland Chinese companies. In total, we estimate that Chinese companies secured 400,000 square feet (37,160 square metres) of office space in Hong Kong under new leases in 2015. In contrast, we calculate that flexible working space operators have secured 252,000 square feet (23,400 square metres) of space in Hong Kong over the first five months of 2016 alone. This figure is equivalent to 63% of the total additional space occupied by Chinese companies in Hong Kong last year.

<table>
<thead>
<tr>
<th>Name</th>
<th>Size (sq ft)</th>
<th>Size (sq m)</th>
<th>District</th>
</tr>
</thead>
<tbody>
<tr>
<td>WeWork</td>
<td>90,000</td>
<td>8,361</td>
<td>Causeway Bay</td>
</tr>
<tr>
<td>WeWork</td>
<td>60,000</td>
<td>5,574</td>
<td>Wan Chai</td>
</tr>
<tr>
<td>TEC</td>
<td>30,000</td>
<td>2,787</td>
<td>Central</td>
</tr>
<tr>
<td>Spaces(Regus)</td>
<td>30,000</td>
<td>2,787</td>
<td>Causeway Bay</td>
</tr>
<tr>
<td>Eaton House</td>
<td>15,000</td>
<td>1,394</td>
<td>Central</td>
</tr>
<tr>
<td>TheDesk</td>
<td>8,000</td>
<td>743</td>
<td>Kennedy Town</td>
</tr>
<tr>
<td>Campfire</td>
<td>8,000</td>
<td>743</td>
<td>Kennedy Town</td>
</tr>
<tr>
<td>Urban</td>
<td>6,000</td>
<td>557</td>
<td>Central</td>
</tr>
<tr>
<td>Metta</td>
<td>5,000</td>
<td>465</td>
<td>Central</td>
</tr>
<tr>
<td>Total</td>
<td>252,000</td>
<td>23,412</td>
<td></td>
</tr>
</tbody>
</table>

Source: Colliers. Note. We have excluded a deal to occupy 140,000 square feet of space in Sai Ying Pun by Soho House, which is a private members’ club.

The expansion of flexible working space operators so far in 2016 has been less concentrated in Hong Kong’s prime locations than has been the case for expansion by Chinese companies. Nevertheless, the flexible working space operators have certainly had an impact on the prime areas. The map below shows that just-under one-third of centres (i.e. sites) occupied by flexible working operators in Hong Kong are located in the core districts of Central and Admiralty. All of the others are in established or emerging commercial locations.

Location of coworking operators within Hong Kong: centres as % of total

WeWork has been the force behind the most eye-catching expansion deals by flexible working operators in Hong Kong so far in 2016: the company has secured 150,000 square feet of office space in the territory,
including 90,000 square feet in a brand new Grade A office building located at 535, Jaffe Road in Causeway Bay. However, it is noteworthy that WeWork has leased about two-thirds more space in Shanghai than in Hong Kong this year – a total of 250,000 square feet or 23,200 square metres in total. This total is split between three locations, two in the Jing’an district and one in Huangpu.

If flexible working space operators continue to expand at the same rate in Hong Kong as they have done so far in 2016, then a simple calculation, i.e. \((252,000/5\times12)\), suggests that they may end up securing 605,000 square feet (56,200 square metres) of space in total this year. This figure would be 60% higher than the aggregate space occupied under new leases by Chinese companies in Hong Kong last year. In reality, we doubt very much that flexible working space operators will occupy so much space, partly because the total for the first five months includes two huge deals by WeWork which are unlikely to be repeated on the same scale, and partly because very limited supply of new office buildings in Hong Kong ought to constrain the operators’ ability to fulfil their ambitions. Still, we confidently predict that flexible working operators will take up at least 475,000 square feet (44,100 square metres) of office space in Hong Kong in 2016. This would still be nearly 20% more than the total additional space secured by Chinese groups in Hong Kong in 2015.

Based on Colliers’ data, the new space occupied by Chinese companies in Hong Kong in 2015 accounted for 1.1% of total Grade A and Grade B office stock of 37.3 million square feet (3.45 million square metres) in the core and fringe CBD areas of Central, Admiralty, Wanchai, Causeway Bay and Sheung Wan. While this may not sound like a high proportion, there seems little doubt that Chinese companies represented a strong source of new demand for office space in Hong Kong last year – as they continue to do this year. We believe that this factor helped to support rents in the core areas of Hong Kong in 2015.

If our estimate that flexible working operators will take up 475,000 square feet (44,100 square metres) of office space under new leases in Hong Kong in 2016 is correct, then this year they will occupy space equivalent to 1.3% of the total office stock in the core and fringe CBD areas of Hong Kong. Again, while this may not sound like a high proportion, at the margin it should be sufficient to ensure that demand for office space remains very firm. In turn, this factor should ensure that vacancy levels remain low and ultimately underpin rent levels.

Is the strong growth in supply of flexible working centres matched by demand from end-users for the space? We think that it is. In fact, there has been rapid growth in demand for coworking space in Hong Kong. An online questionnaire by StartmeupHK in August 2015 covering the managers of 24 coworking space sites and six incubator and accelerator operations showed that 1,558 start-up businesses were located in their workspaces, an increase of 46% from one year earlier. (1) See http://www.startmeup.hk/en/one-stop-hong-kong/startup-ecosystem-survey/

In addition, the survey showed that, out of a total of 1,912 entrepreneurs, 36% had founded their start-up ventures in publicly funded coworking centres, incubator or accelerator operations, while 64% were located in private facilities. This fact suggests that there would be strong growth in demand for flexible working space in Hong Kong even in the absence of government support.

We think that pure coworking space still only occupies 1-2% of core and fringe CBD office space in Hong Kong. Furthermore, while about two-thirds of flexible working centres are located in office buildings, the sites leased are generally small, with the majority below 10,000 square feet or 929 square metres. In our opinion, this fact should not disappoint landlords of Grade A office buildings, or deceive them into failing to take the trend towards flexible working space seriously. This is because we expect the flexible working space market in Hong Kong to be increasingly dominated by international groups which can afford to take space on a larger scale than local operators.

![Image](http://www.startmeup.hk/en/one-stop-hong-kong/startup-ecosystem-survey/)

In our opinion, this fact should not disappoint landlords of Grade A office buildings, or deceive them into failing to take the trend towards flexible working space seriously. This is because we expect the flexible working space market in Hong Kong to be increasingly dominated by international groups which can afford to take space on a larger scale than local operators.

**Occasion of HK office space by Chinese groups in 2015 and flexible working operators in 2016**

<table>
<thead>
<tr>
<th>Space secured under new leases (sq ft)</th>
<th>As % of total core and fringe CBD Grade A &amp; B office stock</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mainland Chinese tenants in 2015</td>
<td>Flexible working operators in 2016 (estimated)</td>
</tr>
<tr>
<td>400,000</td>
<td>475,000</td>
</tr>
<tr>
<td>1.1%</td>
<td>1.3%</td>
</tr>
</tbody>
</table>

**Source:** Colliers’ estimates
Singapore

Singapore is a major regional financial centre which is increasingly becoming the business start-up launch pad for Southeast Asia. This activity is being driven by the technology sector. Start-up businesses in Singapore benefit from access to affluent consumers and a large base of multinational corporations to scale up their operations. The Singapore government’s USD1 billion Technopreneurship Innovation Fund has offered up to USD2 million per start-up to entrepreneurs in the Asia Pacific region and other parts of the world since 1999. Examples of the strong scaling ability of the Singapore system include success stories such as Garena, a Singapore-based online entertainment and e-commerce start-up founded in the city in 2009 and implicitly valued at USD3.75 billion in March 2016 after a new round of financing led by Malaysia’s state investment firm Khazanah Nasional Bhd.\(^1\) The Global Startup Ecosystem Ranking 2015 published by the San Francisco based research firm Compass ranked Singapore no.10 in the world, up from no.17 in 2014. Singapore was ranked first in Asia although the study actually excluded China, South Korea and Japan.\(^1\) See http://www.wsj.com/articles/singapores-garena-raises-new-funds-valuating-it-at-3-75-billion-1459401017.

We have not found Singapore government data on the number of start-up businesses in the country. According to AngelList, a US online platform that allows start-ups to raise money from angel investors, in May 2016 there were 1,723 start-up businesses in Singapore, which had been growing at a compound annual growth rate of 106% since August 2011. According to Compass, there are 2,400-3,600 active technology start-ups located in the city-state. In view of Singapore’s success as a location for start-up ventures in general and technology start-ups in particular, we believe that Singapore is very well-placed to be the leading fintech hub for South-East Asia. Indeed, we have found that more US based fintech service providers are established in Singapore than in Hong Kong, the city-state’s great regional financial rival.

Start-up businesses tend to involve significant numbers of independent workers, entrepreneurs and freelancers. As such, start-up businesses are especially likely to consider the use of flexible working space. It should therefore come as little surprise that the number of flexible working centres in Singapore has been steadily increasing. Since Hackerspace, Singapore’s first coworking centre, opened in the Arab Street district in 2009, the number of coworking centres in the city has increased steadily. Based on various internet and press sources, we estimate that there are now more than 40 flexible working sites in Singapore altogether, although only 28 are listed on the listed on the Internet by the website coworkingsingapore.com as of 31 May 2016.

According to the list on this site, the great majority of flexible working centres in Singapore occupy office space of 5,000 square feet (465 square metres) or below. Only large operators such as The Hive, The Working Capitol and JustCo occupy office space in a range of 12,000-30,000 square feet (1,115-2,790 square metres). In 1Q 2016, a local flexible working provider called The Great Room leased 15,000 square feet (1,395 square metres) of space on Level 10 of One George Street, a class A office building sky in Raffles Place in Singapore’s downtown core. However, most other flexible working centres in Singapore are located outside the city’s central business areas.

**Distribution of flexible working centres in Singapore by space occupied (square feet)**

<table>
<thead>
<tr>
<th>Number of firms</th>
<th>Number of firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,500-2,500</td>
<td>12</td>
</tr>
<tr>
<td>2,501-5,000</td>
<td>5</td>
</tr>
<tr>
<td>5,001-10,000</td>
<td>6</td>
</tr>
<tr>
<td>10,001-15,000</td>
<td>2</td>
</tr>
<tr>
<td>15,001-25,000</td>
<td>1</td>
</tr>
<tr>
<td>&gt;25,000</td>
<td>1</td>
</tr>
</tbody>
</table>

Source: coworkingsingapore.com; Colliers

Property developers in Singapore have been reacting to the potential for continued growth in the flexible working space market. For example, Keppel Land has introduced a 6,400 square foot (595 square metre) hybrid serviced office and coworking space at Keppel Towers in the Tanjong Pagar financial district of central Singapore. Similarly, in March 2016 CapitaLand started offering premium coworking space as part of its pilot initiatives to test alternative working spaces at Capital Tower, its Grade A office building also located in Tanjong Pagar.
We should mention that the Singapore government has also been involved in providing new flexible working space. One example is the establishment of JTC Launchpad @ one-north. This is a coworking enclave for start-up ventures and incubator operations in the communications, media, biomedical sciences, electronics and engineering industries. JTC Launchpad @ one-north is located outside the Singapore CBD on Ayer Rajah Crescent, where it occupies three entire blocks with capacity of 430,000 square feet (39,960 square metres). The enclave currently hosts 40 incubation centres and 600 start-up operations with plans for the latter number to rise to 750 by 2017.

China

We hope we have made clear our view that there is firm demand for flexible working space in China. This is particularly true in Beijing where Zhongguancun is China’s key hub for technological innovation. However, China in general has seen strong growth in recent years in demand for mobile communications and internet services. Indeed, China is now home not only to some of the world’s largest internet businesses, groups such as Alibaba (e-commerce) and Tencent (China’s largest portal) with market values of USD191bn and USD207 billion respectively, but to a wide range of much smaller technology companies and entrepreneurial start-ups. Moreover, China has established itself as a leader in Asia in the emerging fintech sector; please see the Appendix for more details. While the technology sector is far from the only source of demand for flexible working space, it is one of the most important.

What about supply of flexible working space? SOHO 3Q, URwork and People Squared are established flexible working operators with high market shares. We do not know the total office space occupied by SOHO 3Q, which we believe to be the largest of these players. However, we understand that SOHO 3Q runs 12 flexible working sites in the two cities and that it is currently providing over 10,000 desks, with an ambition of raising that total to 100,000 by 2017 (according to a statement from SOHO China’s Chairman reported by Bloomberg on 8 December 2015). We know, moreover, that SOHO 3Q only offers space within SOHO China’s own offices, which are all located in Beijing and Shanghai. We suspect that SOHO 3Q’s ambitious desk expansion target is only achievable because SOHO China’s office properties are generally non-Grade A office buildings.

URwork is based in Beijing and provides business incubation services. URwork has also been expanding fast with more centres due to be opened in Beijing, Shanghai and second-tier cities. People Squared is operating in 14 locations across Beijing and Shanghai.

According to an article in the South China Morning Post(1) on 28 March 2016, URwork received more than RMB200 million (USD30 million) in a new round of funding in March. This funding raised the private company’s implied valuation RMB4.0 billion or USD610m, providing the company with ample resources to pursue expansion plans. Similarly, Kr Space, a Beijing-based private business incubation company which has recently raised funds independently from its parent group 36Kr, reached an implied valuation of RMB1.0bn (USD150m) on 25 January 2016. However, Kr Space does not yet seem to be in the league of the other flexible working operators, with only one site in Zhongguancun at present.

Notwithstanding the strength of the local players and the competitive nature of the Shanghai and Beijing markets, certain international flexible working space operators see China as an attractive market for expansion. As noted earlier, WeWork of the US has leased 150,000 square feet or 14,870 square metres of space in Hong Kong so far in 2016. However, WeWork has leased two-thirds more space in Shanghai than in Hong Kong – 250,000 square feet or 23,200 square metres in total. This space is split between three locations, two in the Jing’an district and one in Huangpu.

On balance, we think that the entry of international flexible working space operators like WeWork will have a less disruptive near-term impact on the office markets in Shanghai and Beijing than in Hong Kong. We base our view partly on the strength of the local players and the greater volume of office stock available in the mainland Chinese cities. Furthermore, the flexible working operators in China are very cost-sensitive and usually cannot afford the rental payments in the Grade A office segment; they therefore normally choose non-Grade A properties in non-prime locations. For this reason we do not anticipate that flexible working operators will have a significant impact on the Grade A office market in Shanghai or Beijing, especially in the CBD segment. However, flexible working operators probably will help to enrich the tenancy mix and boost occupancy in the decentralised business district and business park areas.

Implications for property market players

Expansion in market set to continue

We expect the factors driving the desire for more flexible working space to continue to strengthen. These factors represent global trends, and are eliciting global responses by players in the property sector – including property services groups such as Colliers, which has, for example, established a Coworking Advisory Services team in the US. One estimate (Deskmag’s 2016 Coworking Forecast) calls for the total number of coworking centres globally to increase by 63% over 2016 from 7,800 to 12,700, and we expect Asia to be a driving force behind this growth.

What are the implications of this continuing growth for the major participants in property markets in Asia – landlords and developers, occupiers and investors? We summarise our opinions below.

Landlords can expect higher demand for space, but must build relations with a new class of tenant

To the extent that flexible working operators are emerging as major new sources of demand for office space, the first implication of the new trend for landlords is that they can expect increased competition for space which should underpin rent levels and perhaps push them upwards. This is most likely to be true in Hong Kong. Over the past year or so, demand for space from Chinese companies has certainly helped to mitigate pressures on the traditional large tenants in Hong Kong Central, global banks and investment banks, to downsize and vacate surplus space. Although demand from flexible working space operators has been less concentrated in the prime districts, it is another factor which has supported demand for office space overall. We expect demand to remain very firm in the near term.

We should not overstate the potential for demand from flexible working space operators to underpin office rents or push them upwards. Flexible working space operators are in a good position to negotiate long rent-free periods with landlords, partly because they do not need to wait for an existing lease to expire before committing themselves to a new lease. Then again, many flexible working operators are moving towards
Developers should incorporate new features into building design

For the original developers of office buildings (which may or may not be the same as the subsequent landlords), one obvious implication of the growing popularity of flexible working space is the need to incorporate new features into building design. Notably, flexible working operators tend to seek large floorplates with plenty of natural light, because these qualities improve the working environment for the end-users. In markets where flexible working is becoming popular, developers which do not include these features adequately in building design risk missing the opportunity to attract a major new class of potential occupier.

More fundamentally, we would argue that developers need to engage flexible working operators earlier in the building development cycle as the latter may well constitute a large tenant group in the future. This implies that developers need to think hard about building positioning and future tenant mix to ensure that flexible working operators and other tenant groups can happily coexist.

Coworking occupants in Hong Kong and Singapore should look for space in the CBD fringe or outside it; China will be tough to penetrate

Quite what occupiers are in the context of flexible working space is an important question. We tend to think of the occupiers as flexible working operators themselves, since they will be the parties signing lease agreements, rather than their clients or “members”. The latter group is likely to include both employees of companies and individuals, but in either case they have a business relationship with the flexible working operator rather than the landlord of the building.

In this context, we should stress again that Hong Kong and Singapore are currently home to around 40 flexible working space operators each. The distribution of the existing operators thus provides clues about how new entrants should move into the market. In our view, smaller flexible working operators and start-ups in the field should look for office space in decentralised districts, whereas established operators should look for space in CBD fringe areas. Due to high office rents in the two cities, non-grade A office buildings within the core CBD are another option for established operators to consider.

International flexible working operators should find themselves quite competitive in Hong Kong and Singapore, given their experience abroad and –

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**Spread of coworking space: positives and negatives for landlords**

- Pre-Lease of Space
- Large Space Users
- Concept Selection
- Range of space options in the building
- Amenities to existing Tenants
- Disruptive
- Common Area Use
- Concept Selection
- Impact on Tenant Mix
- Lack of control

Source: Colliers International

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**Impact on Tenant Mix**

- Core CBD are another option for established operators
- The latter group is likely to include both employees of companies and individuals
- For the original developers of office buildings (which may or may not be the same as the subsequent landlords)
- This implies that developers need to think hard about building positioning and future tenant mix to ensure that flexible working operators and other tenant groups can happily coexist.

**Core CBD**

-Where established operators should look for space
- Due to high office rents in the two cities
- Non-grade A office buildings within the core CBD are another option for established operators to consider.
Hopefully – reasonably strong financial positions. By contrast, in China there are several well-established domestic flexible working operators with high market share. The three largest established domestic firms operate in 10-20 centres in Beijing and Shanghai, albeit mainly in non-prime locations, and are continuing to expand. We expect that international operators will find it tough to make major inroads into the Beijing and Shanghai markets.

**Investors should watch operators’ business models, because over-expansion on a localised scale is a risk**

For property market investors which are also landlords, again the first implication of the growing popularity of flexible working space is that they can expect office rents to be supported, and perhaps pushed upwards, by increased competition for space reflecting demand from a major new class of tenant. Conversely, demand for flexible working space should not lead to significant upward pressure on office property capital values, because flexible working operators are not engaged in the business of buying buildings outright.

Over the medium to long term, property investors – like landlords and developers – should pay careful attention to the business models of serviced office and flexible working operators, and ensure that the operators’ cash flows are adequate to cover both their rent obligations and their capital expenditure requirements. We have no doubt that the trend towards flexible working space is here to stay, both globally and in much of Asia. However, the high interest of private equity capital in flexible working operators raises the question whether the potential risks of investment in the sector are being assessed as carefully as the potential rewards. We do see a risk of over-expansion on a localised scale by flexible working operators. If operators find that they cannot generate sufficient revenue from their end-user clients to cover their cash expenses, then they may have to rationalise by closing flexible working sites and releasing the space. In extreme scenarios, bankruptcies among operators are conceivable. This raises the possibility of a glut of empty office space appearing in certain districts, pushing down rental levels and maybe capital values in those areas.

In our view, this risk of over-expansion applies particularly to those flexible working space operators focusing on the low end of the market, where the end-users may be little more than tourists. (Some flexible working centres in markets such as Thailand, for example, are becoming centres for tourists who are travelling and still need to contact their companies or undertake business.) The risk applies less to an operator like Servcorp, which usually only occupies top-grade buildings in prime CBD locations.
Appendix: new technology helps drive demand

Many different industries are contributing to growing Asian demand for coworking space. However, we have mentioned two sectors which stand out. The first is fintech (financial technology), for which we expect investment in the Asia Pacific region at least to treble this year to USD15.2 billion. The second is the so-called Internet of Things.

Fintech

Structural changes in the traditional banking sector and the demand for innovative financial services have created significant growth in the fintech industry. According to the report Fintech and the Evolving Landscape: Landing points for the industry structure (April 2016) by the consultancy Accenture, total global investments in fintech stood at USD22.3 billion in 2015, an elevenfold increase from 2010. The report also estimates that total fintech investments in the Asia Pacific region in 2015 amounted to USD4.3 billion, and in the first quarter of 2016 to USD2.7 billion.

Moreover, Ant Financial Services Group, the operator of Alipay, a major online payments platform in China, raised USD4.5 billion in its second round of fintech funding in April this year. The amount raised is more than the combined fintech investments in Asia Pacific in the whole of 2015.

Taking into account the 2016 Asia Pacific fintech investments so far, including a USD1.2 billion funding round by the Chinese online lending platform Lufax in January and last month’s Alipay fundraising exercise that reached USD4.5 billion, we predict that aggregate fintech investments in the region in the first half of 2016 will reach USD7.7 billion, with 2Q alone accounting for USD5.0 billion. Looking into the second half, we expect to see investment volume of USD3.5 billion in 3Q. This would represent a 30% decrease from the arguably exceptional 2Q level, partly reflecting the Chinese government’s current push to strengthen regulation of the online finance industry which may discourage increasing speculative investment in this area, including peer to peer lending. For 4Q 2016, we assume investment volume of USD4.0 billion. Hence, we estimate that total investment in Asia Pacific will increase by over 250% in 2016 to USD15.2 billion.

Looking ahead beyond 2016, it is difficult for us to make precise projections about how fast the fintech sector may continue to grow. However, considering both the almost universally strong interest in digital and internet-based financial solutions and the potential for fintech to help streamline financial institutions’ cost bases, we are very confident about fintech’s ongoing expansion potential. In addition, we have underlined the fact that substantial investment in fintech is taking place in China, where the internet sector and e-commerce in particular have achieved remarkable growth in recent years. In our opinion, the probability of a soft economic landing in China has increased recently, due in particular to significant growth in services and light industry. This growth is helping to mitigate well-known problems such as a high national debt/GDP ratio and overcapacity and margin compression in heavy industry.

Assuming both continued significant expansion in the fintech industry per se and a soft economic landing in China, we tentatively predict growth in total fintech investment in Asia Pacific of 20% in 2017, to USD18.2 billion, and of a further 10% in 2018, to USD20.0 billion. The success of the fintech sector in Asia Pacific so far in 2016 might make these projections seem almost conservative. Conversely, they would be vulnerable to possibly very substantial downward revision in the event of a Chinese hard economic landing or – still worse – a renewed global economic slowdown.

We should note that Singapore and, indeed, China (which is home to some of Asia’s largest fintech operations) are well ahead of Hong Kong in fintech development. The representative of Fintech Hong Kong, an organisation bringing fintech start-ups, community and events together, believes that a lack of appetite, mind-set and culture to build or work for start-ups is the major reason why fintech development in Hong Kong is still at an early stage. The Hong Kong government has recognised the importance of its support for further
fintech growth: it established an Innovation and Technological Bureau in 2015 and has set up a HKD2 billion fund to encourage progress in these areas.

**Internet of Things**

Internet of Things (IoT) stands for the network of physical objects embedded with electronics, software, sensors, and network connectivity that enables these objects to collect and exchange data. According to the report *The Internet of Things: Mapping The Value Beyond The Hype* (June 2015) by the McKinsey Global Institute, the economic impact of IoT applications could be as much as USD7 trillion by 2025. Another report *Forecast: The Internet of Things, Worldwide, 2013* by Gartner, predicts that IoT vendors will earn more than USD309 billion by 2020. Cisco IBSG’s research paper *The Internet of Things - How the Next Evolution of the Internet Is Changing Everything* predicts there will be 50 billion devices connected to the Internet by 2020.

There is particular scope for IoT operations to expand in Asia. The ITU, the United Nations’ specialised agency for information and communication technologies, calculates that the internet penetration rate has increased at an average rate of 2.8% per year in Asia to the end-2015 level of 36.9% in 2015, similar to the penetration rate in the Americas in 2005.

In Hong Kong, the government has also addressed the importance of IoT in its policy agenda. It has set up incubation centres and has been encouraging venture capital investment to support IoT businesses. Start-up ventures in information, communications and technology, and in IoT applications, account for the two highest totals of start-up enterprises in Hong Kong (see table below).

![Regional Internet Penetration Rate](image)

**Source:** ITU

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**Hong Kong Entrepreneur Sector Distribution**

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<tr>
<th>Sector</th>
<th>No. of entrepreneurs 2014</th>
<th>No. of entrepreneurs 2015</th>
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<tbody>
<tr>
<td>Information, Computer &amp; Technology</td>
<td>273</td>
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<tr>
<td>Hardware (IoT, prototypes, wearables)</td>
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<td>48</td>
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<tr>
<td>E-commerce/ Supply Chain Management</td>
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<td>77</td>
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<tr>
<td>Professional or Consultancy Services</td>
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<td>106</td>
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<tr>
<td>Design</td>
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<tr>
<td>Education &amp; Learning</td>
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<td>57</td>
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<tr>
<td>Financial Technology (Fintech)</td>
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<td>74</td>
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<tr>
<td>Health &amp; Medical</td>
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<tr>
<td>Data Analytics</td>
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<tr>
<td>Gaming</td>
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<td>Sustainable Technology</td>
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<tr>
<td>Others/don’t know</td>
<td>26</td>
<td>26</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>217</strong></td>
<td><strong>195</strong></td>
</tr>
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</table>

**Source:** StartmeupHK
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