Yardi Matrix

National Office Report

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Flex Space and the Future of Office

- The last two years have been tumultuous for the office sector as millions of workers have remained remote and businesses have sought to reevaluate office footprints. While there has been much speculation as to whether remote work will become permanent, firms still need physical space for training, collaboration and culture building, and flex space is emerging as a solution.

- In the near term, flex space can bridge the gap between an uncertain future and the needs of the present. In the long term, shared space will play a vital role in providing the flexibility that is crucial to attracting and retaining employees in a tight labor market. Flex space allows firms to offer their workers offices and amenities while keeping real estate costs lower than a traditional lease. Earlier this year, a CBRE survey of 77 global companies revealed 86% will include flex space as part of their real estate strategies going forward. Only 5.6% of office buildings have a flex space within their properties, according to Yardi Matrix, and most of those buildings are highly clustered in the largest markets. More than 30% of buildings with flex space are in just five markets—Manhattan, Los Angeles, Washington, D.C., Dallas and Boston.

- Going forward, it is less likely that flex space operators will use the revenue model common before COVID-19, where operators signed leases for high-quality space in city centers and then rented the space out to their members. We expect franchising and management agreements with revenue sharing to become more common. In management agreements, landlords will be responsible for the cost of fit-outs but are able to receive a larger share of the revenue from the operators. These agreements also reduce the risk of leasing to a single flex space tenant and align incentives between the operators and landlords.

- WeWork, which had a successful(-0.3%) IPO this year through an SPAC two years after its failed IPO led to turmoil at the company, has been the most aggressive at exploring new revenue models. It recently entered into a partnership with Saks Fifth Avenue to convert some retail space into flex space. WeWork has also received a $150 million investment from Cushman & Wakefield with an agreement to combine its hospitality and technology services with Cushman's asset and facilities management services. Other real estate service firms are also taking an interest in operating shared spaces. This year, CBRE acquired a 35% stake in Industrious and Newmark purchased Knotel out of bankruptcy.