

# Disruption *or* Distraction

Where next for the UK flex space market?

# UK Disruption or Distraction - Key Points

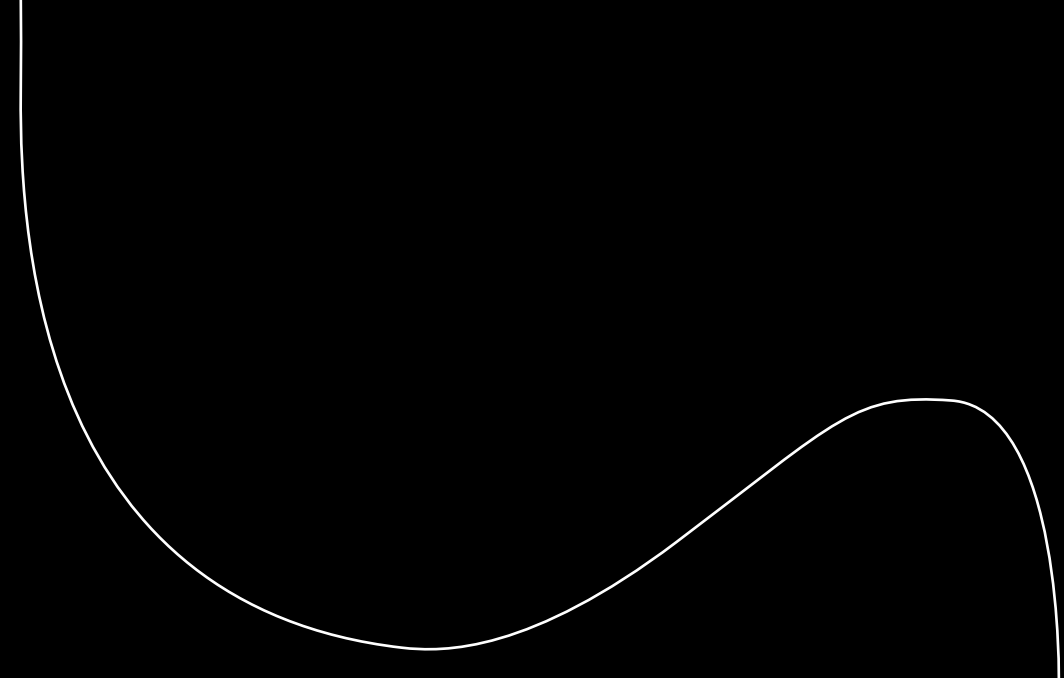
## Key points

- London's growth rate is slowing while regional growth is accelerating but business models are stretched in many environments
- There will be a convergence between flex space and conventional space increasing focus on services and flexibility combined with the rise of CAT A+/CAT B
- There will be more management agreements and partnerships rather than landlord only models driven by competition in London and by economics in other cities
- Data and analytics may be the next space in which landlords and individual flex operators compete
- Investors are increasingly accepting of this model, given that they are more accommodating of operational real estate but that may mean;
  - different valuation approaches using cash flow rather than yield
  - valuations based on the perceived ability / creditworthiness of the operator

## Background

The flex space market is becoming a significant part of the UK office market, with growth from both new entrants and established operators expanding rapidly. Meanwhile, investors' growing acceptance of the sector has resulted in record flex leasing activity and more landlord delivered models.

This growth is being driven by the evolving nature of work and the shifting structure of the economy, supported by rapidly advancing technology. The UK<sup>1</sup> flex space footprint grew by almost 4.0 million sq ft during 2018, the strongest increase on record. Nevertheless, it still represents a small part of the overall office market, accounting for just 5% of stock.



<sup>1</sup> Refers to Central London, Belfast, Birmingham, Bristol, Cambridge, Cardiff, Edinburgh, Glasgow, Leeds, Liverpool, Manchester, Newcastle, Nottingham, Sheffield and the Western Corridor

## Regional growth

London has led the way, but the regional cities have also seen a surge in flex space leasing activity over recent years. Take-up in the Big 6 cities<sup>2</sup> rose 26% between 2017 and 2018 to reach close to 600,000 sq ft (10% of overall take up), although this is behind Central London, with 1.9 million sq ft (17% of the total).

The pattern of take-up in the Big 6 is following a similar trajectory to Central London, but lags by around three years – meaning that activity looks set to intensify in the medium term. Over the next five years more than 10 million sq ft could be added to the UK market, pushing the total market size to around 30 million sq ft or 8.5% of total stock.

Operators are expanding their footprints into new markets and this trend will accelerate. The focus is on the core regional cities, which already have an established office market with untapped demand but the lower return on investment than in London means that some secondary cities are financially out of the reach of some operators.

## Evolving business models

Most operators are developing a hybrid model, offering both private offices and co-working spaces. While there is still space for a traditional serviced office model, the rapid expansion of this model means that it already accounts for nearly half of all flex space, and changing customer demands suggests that it will continue to dominate the growth of the market over the next few years.

Search data from Hubble<sup>3</sup> clearly supports the surge in demand from larger users, with searches for more than 50+ desks recording fastest year-on-year growth, and the focus on demand for private office space.

But customers want the added benefit of communal and collaboration space in the centre, as well as a sense of community. Amenity space has become a more important element of the offer, but the provision of co-working space is often a loss leader designed to energise communal spaces.

Providers are disrupting the property sector by introducing new levels of customer service and intelligence - taking lessons from the retail and hospitality sectors. Service is at the forefront of the business model, it helps to differentiate the product, enables the customer to operate more productively and boosts retention rates. Data and analytics will allow operators to understand how companies use their space and to evolve their product accordingly.

The next phase of service provision will centre on “managed workspace” provided by flex operators, where space is tailored to the individual occupier’s requirements. These typically command longer lease terms – around five years – and is leading to a blurring between the offer from the traditional landlord and flex operators.

As the market develops and the focus on client service intensifies, there will be a polarisation between the larger players and niche operators, with increasing specialisation according to local business mix and culture.

## Landlords’ response

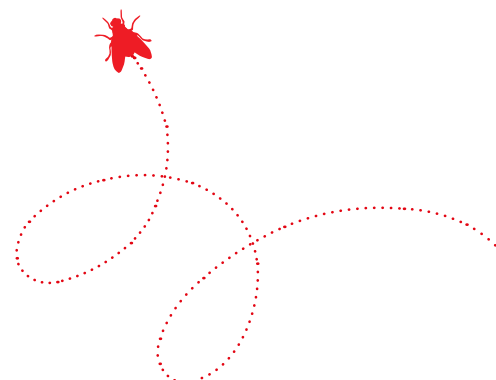
Landlords are being forced to consider what the rise of the sector means for their portfolio and how to ensure that space remains relevant and delivers the best returns.

While some will continue to pursue a straight lease to an operator, using flexible workspace to activate leasing velocity and to provide an element of community space, the partnership model is gaining momentum as an alternative solution – similar to the model seen in the hotel sector. We expect this to be the fastest growing route to market in the medium term.

The landlord model is gaining traction, but only those with a large portfolio and skilled resources will be able to seriously enter the marketplace. Landlords are seeking to enrich their total property offer and are looking to gain control as the new wave of flexible workspace providers continues to expand around them. This will remain a relatively small part of the sector.

## Outcome

While the sector has seen significant growth in recent years, it remains in its infancy, especially in the regions. Flex has not yet truly disrupted the office market - there is more to come - and in the future the models of flex providers and conventional landlords will converge. The former will increasingly offer longer leases and court corporate tenants; the latter will offer more flexibility, amenities and rentalised “Cat A+/Cat B” fit-out.



<sup>2</sup>Birmingham, Bristol, Edinburgh, Glasgow, Leeds & Manchester

<sup>3</sup>Hubble is a platform to search, view and book shared offices, coworking spaces and serviced office space in London and Manchester

# Contacts

---

**Ben Munn**

Managing Director, Flexible Space

**[ben.munn@eu.jll.com](mailto:ben.munn@eu.jll.com)**

+44 (0)20 7852 4157

**Robin Pugh**

Head of Flex Space Innovation

**[robin.pugh@eu.jll.com](mailto:robin.pugh@eu.jll.com)**

+44 (0)20 7087 5115

+44 (0)7754 747 173

**Elaine Rossall**

Head of UK Offices Research

**[elaine.rossall@eu.jll.com](mailto:elaine.rossall@eu.jll.com)**

+44(0)20 3147 1666

+44 (0)7793 808 319

**Jon Neale**

Head of UK Research

**[jon.neale@eu.jll.com](mailto:jon.neale@eu.jll.com)**

+44 (0)20 7087 5508

+44 (0)7800 874 733



**[flexspace.jll](https://flexspace.jll.com)**

© 2019 Jones Lang LaSalle IP, Inc. All rights reserved. The information contained in this document is proprietary to JLL and shall be used solely for the purposes of evaluating this proposal. All such documentation and information remains the property of JLL and shall be kept confidential. Reproduction of any part of this document is authorized only to the extent necessary for its evaluation. It is not to be shown to any third party without the prior written authorization of JLL. All information contained herein is from sources deemed reliable; however, no representation or warranty is made as to the accuracy thereof.