

Commercial real estate - Russia

CO-WORKING: THE SECRET OF SUCCESS

2ND EDITION
MARCH 2019

Research Department Cushman & Wakefield



KEY TRENDS ON THE FLEXIBLE WORKSPACE MARKET

MARCH 2018 – MARCH 2019

- In 2018, the flexible workspace market increased by 40% - 37,000 sq. m were added to the market. The largest openings of the year: SOK Arena Park, SOK Gardens of Beijing, Tablica, SREDA Federation, CEO Rooms Empire.
- In Q1 2019, 9,000 sq. m of flexible workspace were opened.
- WeWork will become one of the largest operators on the flexible workspace market after opening of 3 locations in Moscow in 2019. At the moment, Regus is the largest operator by occupied area.
- In 2018, Regus was in the process of business optimization - 4 flexible spaces in different parts of the city were closed and one new location in Vivaldi Plaza was opened.
- From March 2018 to March 2019, the share of chain flexible workspace operators increased from 40% to 70% (by occupied area). As predicted, chain operators are now dominating on the flexible workspace market.

130
'000 SQ. M

**MOSCOW FLEXIBLE
WORKSPACE STOCK,
Q1 2019**

1%

**FLEXIBLE
WORKSPACE AS A
PROPORTION OF
MOSCOW OFFICE
STOCK**

WEWORK

KEY OPENING IN 2019

70%

**SHARE OF CHAIN
OPERATORS**

MAP OF FLEXIBLE WORKSPACES IN MOSCOW

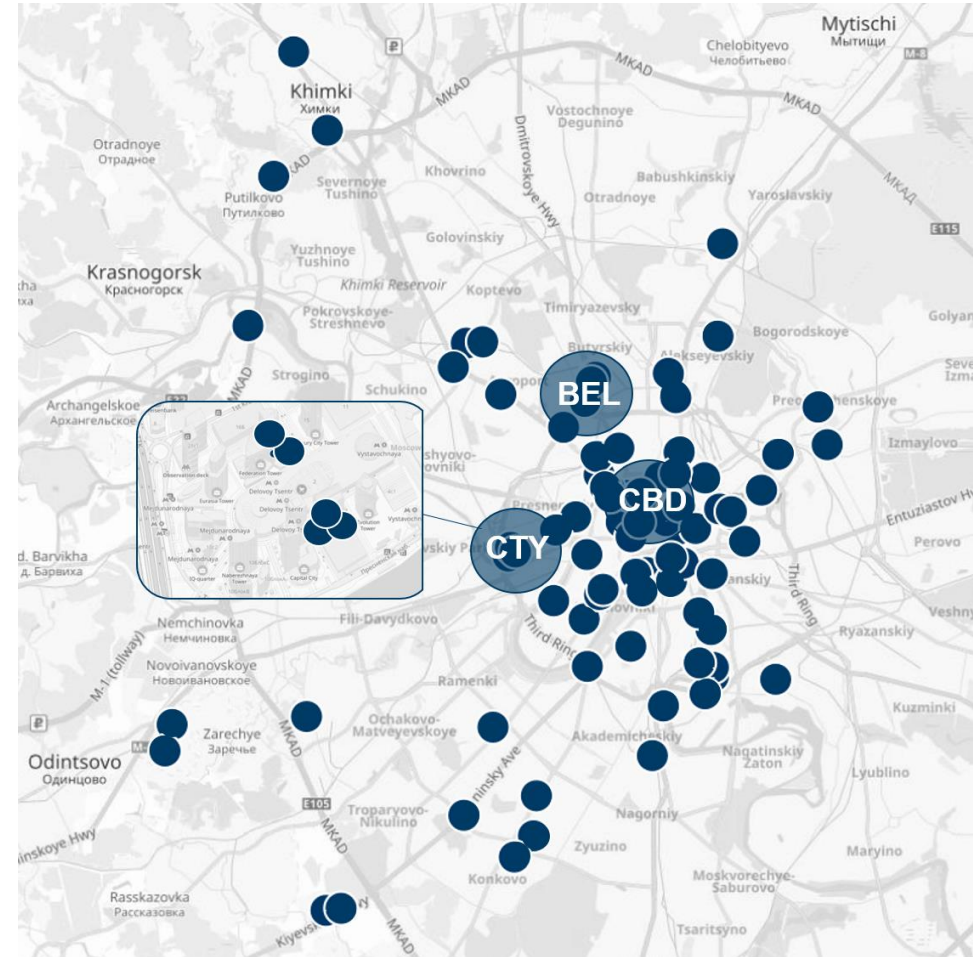
The biggest share of flexible workspaces is located within the Third Transport Ring.

There are **100 dedicated flexible workspaces** in Moscow, 55 of which are chains (55% of the total).

Chain operators often occupy larger spaces than non-chain, so despite a relatively small advantage in number of locations, their share in the total flexible workspace stock significantly exceeds the share of non-chain and comprises 70%.

The majority of flexible workspaces are located in the city center and adjacent areas. Belorussky, Central and City submarkets are the most popular.

One of the major advantages for flexible workspaces is the location in business districts, in walking distance from the metro. The highest demand and occupancy rate are registered in such locations.



MOSCOW IS IN THE TOP10 LARGEST EUROPEAN MARKETS

About 90% of flexible workspace in Russia is located in Moscow.

11

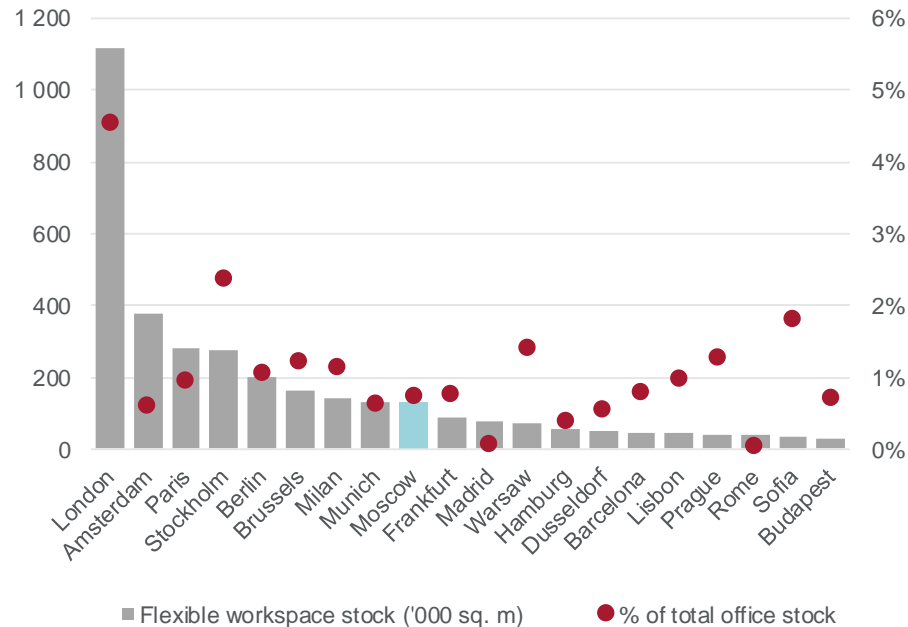
mn sq. m

Global flexible workspace stock

1%

Flexible workspace as a proportion of global office stock

Flexible workspace stock in the key European cities



- The share of flexible workspace in the total office stock in Moscow is **1%**, which is close to global and European average.
- Moscow has the leading position by flexible workspace stock among the capitals of Central and Eastern Europe.
- New York City and London have the largest amount of flexible workspace in the world with over 1 million sq. m each. These two cities alone account for 22% of global coworking stock.



More information on European flexible workspace market can be found in C&W Global Report - **European Hotspot Index**, which is available by the [link](#).

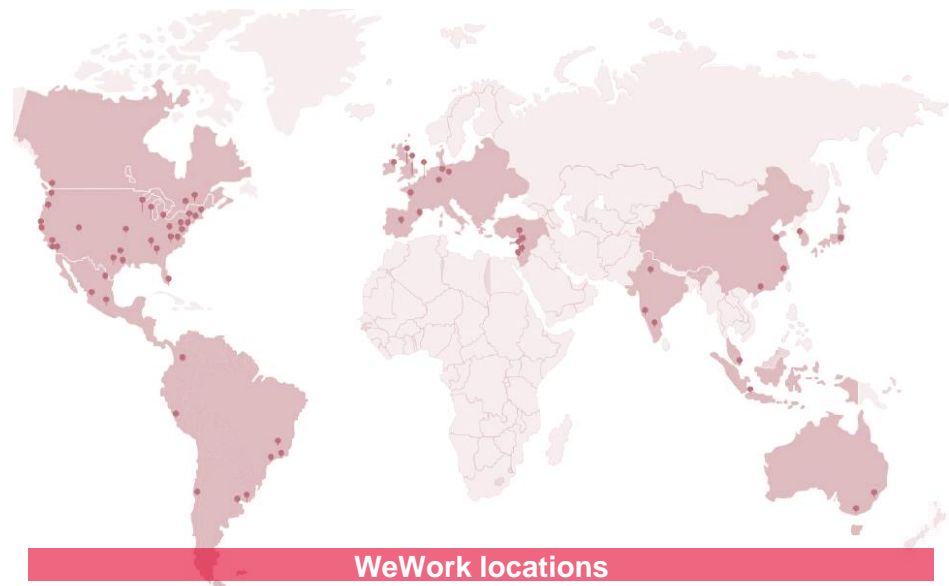


БЦ Белая площадь

- WeWork is the largest flexible workspace operator in the world. The company was founded in 2010 in New York. Currently, there are 425 locations in 100 cities and 27 countries, market value is estimated at 47 bn USD. Around 2.3 mn sq. m of workspace in the world is managed by WeWork.
- WeWork is the largest private office occupier in London, Washington and New York.
- The company is rapidly developing – as of start of 2019, 400,000 people are working in WeWork workspaces, whereas 5 years ago the number of residents was only 7,000 people.

WEWORK – NEW INTERNATIONAL MARKET PLAYER

- Entry of WeWork to the Russian market is one of the highlights of 2019. Currently the only international chain presented in Russia is Regus.
- In 2019, WeWork plans to open three locations in **Moscow**:
 - Krasnaya Roza – 3,950 sq. m, 850 workplaces
 - Yakimanka – 3,600 sq. m, 637 workplaces
 - White Square – 5,400 sq. m, 1034 workplaces
- After the opening in Moscow, WeWork plans expansion to St. Petersburg.

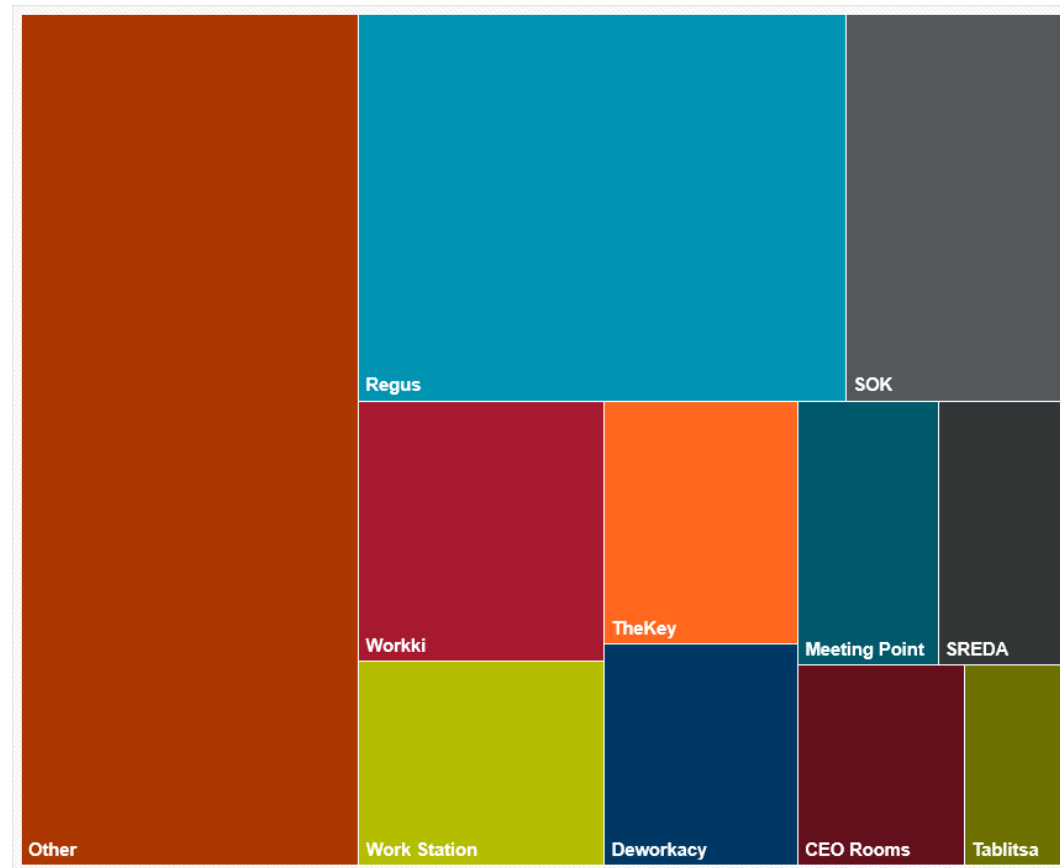
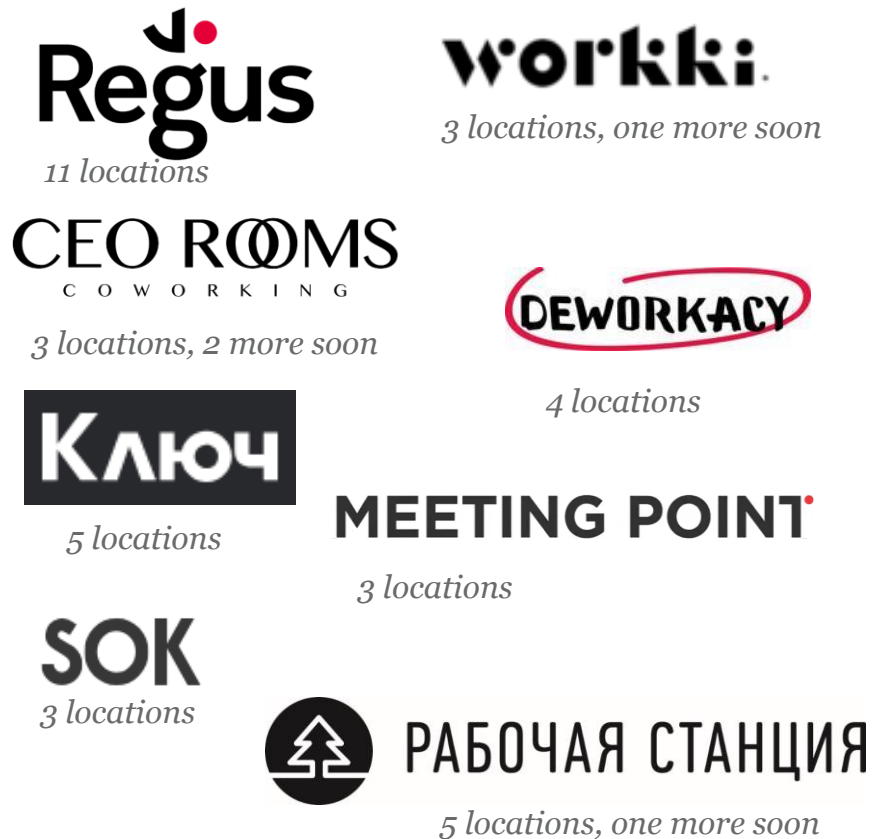


WeWork locations

MAIN MARKET PLAYERS IN MOSCOW

The largest chain operators (with 2 or more locations):

TOP-10 largest flexible workspace operators by area:



MAJOR OPERATORS IN THE MARKET

Chain and independent flexible workspaces with an area of more than 1,000 sq. m

Name	Location	Area (sq. m)	Unassigned desk (RUB)	Assigned desk (RUB)	Mini-office per 1 person (RUB)
WeWork (opening in 2019)	Krasnaya Roza	4,289	24,000		38,000
	Belorusskaya (BC White Square)	5,887			46,000
	Yakimanka 26	3,200			34,000
CEO Rooms	Comcity	1,230	16,500	21,500	20,000
	Empire 16 floor	3,570	35,000	40,000	30,000
	Empire 8 floor	400	35,000	40,000	30,000
	Federation	500		Opening in 2019	
Deworkacy	Izvestia	500	10,000	16,000	14,000
	Polyanka	2,554	10,000	19,000	27,500
	Red October	1,700	10,000	17,000	27,500
	Leont'evskiy pereulok	1,377	10,000	19,000	20,000
TheKey	Arma	1,320	15,900	17,900	from 70,000 for office
	Danilovskaya	1,070	11,900	13,900	from 39,000 for office
	Patriarshie	520	20,900	22,900	from 70,000 for office
	Shelk	1,730	13,900	15,900	from 60,000 for office
	Trekhgorka	1,820	15,900	17,900	from 60,000 for office
	Kuznetsky bridge	600		Opening in 2019	
Cowork Station	Butyrskaya	2,700	14,900	16,900	17,000
	Artplay	700	14,900	16,900	23,000
	Neskuchniy garden	700	14,900	16,900	-
	Balchug	3,081	16,900	19,900	from 25,000 for office
	New location – opening in 2019	4,000		Opening in 2019	
Workki	Federation	2,400	19,900	24,900	31,000
	NeoGeo	2,500	9,900	12,900	15,000
	Komsomolskaya	4,500	11,500	14,900	22,600
	Park of Culture	4,500		Opening in 2019	
SREDA	Federation	4,944	-	30,000	25,000
Tablica	Mendeleevskaya	3,000	16,000	19,000	19,000
Meeting Point	Okhotniy Ryad	1,577	28,000	32,000	from 100,000 for office
	Belorusskaya (BC White Gardens)	2,230	-	-	from 90,000 for office
	Crocus	1,432	15,000	-	from 200,000 for office
	Okhotniy Ryad (potential extension)	7,749			
Regus	11 locations		from 10,500		from 11,500
SOK	Zemlyanoy Val	2,400	16,800	30,000	from 45,600 for office
	Beijing gardens	3,500	16,800	30,000	from 52,000 for office
	VTB Arena Park	6,500	16,800	30,000	from 45,600 for office

(All rents are per month)

LEASE TERMS

Residents of hybrid workspaces have several options when leasing a workplace:

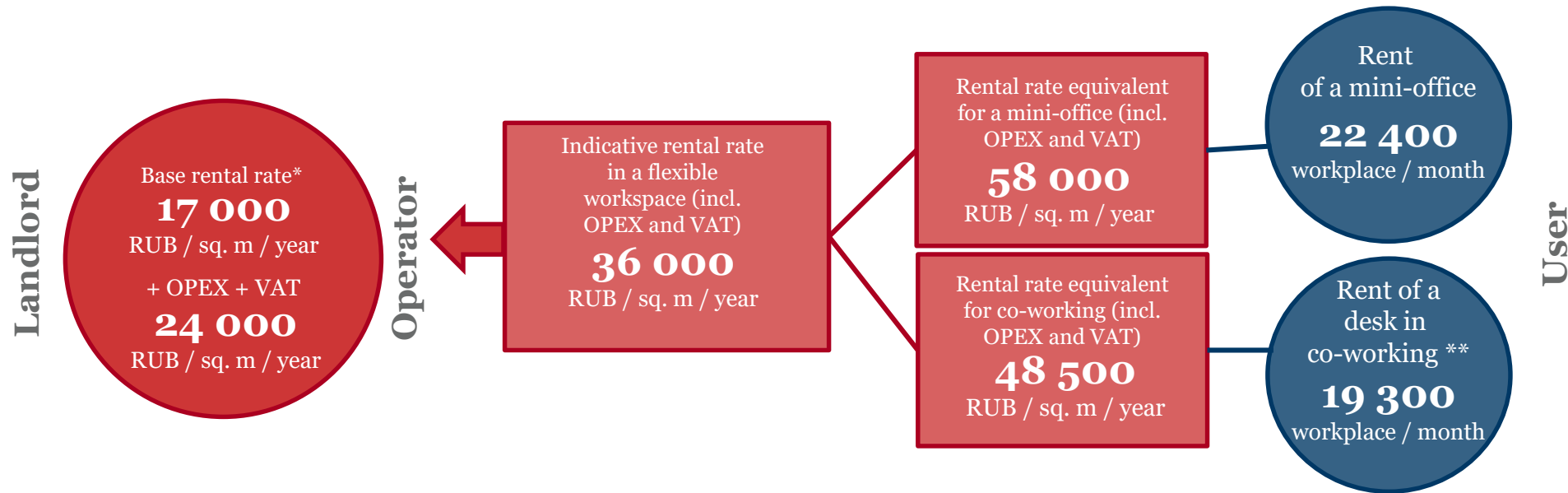
Type of workplace	Standard minimum lease period	Average rental rate, a workplace per month
Unassigned	1 hour	16,200 RUB (~ 246 USD)
Assigned desk	1 month	21,800 RUB (~ 331 USD)
Mini-office	11 months	22,400 RUB (~ 340 USD)

- All rental rates include **operational expenses and VAT**. Rental rates are calculated for chain hybrid workspaces.
- Often rental rates include several hours in meeting rooms. Discounts are sometimes applied for long-term rentals.
- Some flexible workspaces offer co-working passes for several visits per week / month.
- Chain operators generally provide residents with a flexi-pass to work in all their locations.

In 2018, the rental rate growth for desks in co-working areas is more noticeable than for mini-offices (+7% for unassigned desk, +12% for assigned desk). Rental rate for mini-office grew by 5% on average. This increase is caused by newly opened flexible workspaces with higher rental rates.

** Rental Rates in US Dollars are calculated according to the current Russian Central Bank exchange rate (as of 26/02/2019):
1 USD = 65,8 RUB*

INDICATIVE RENTAL RATES

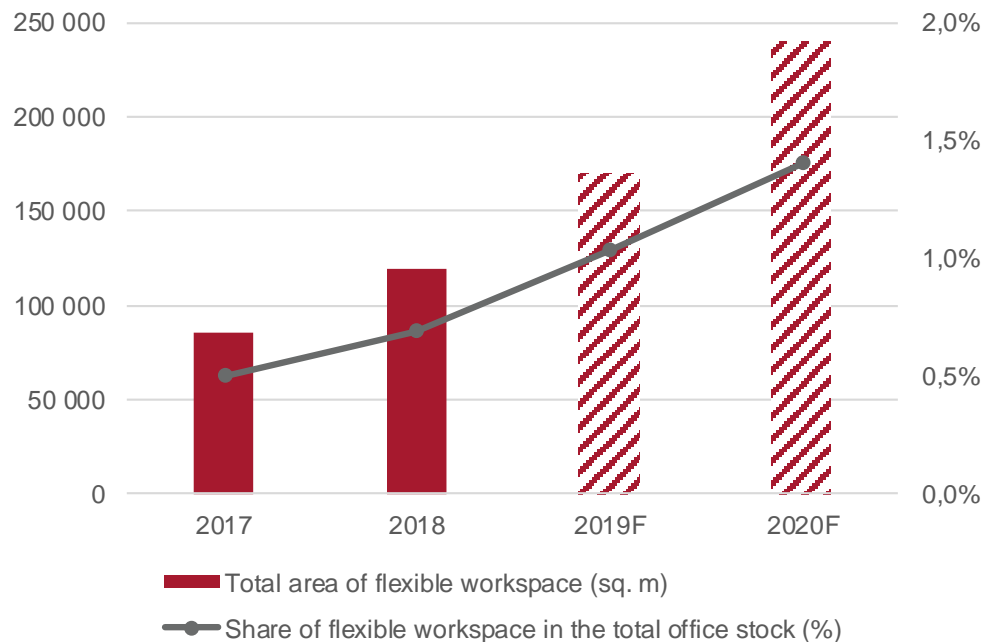


* Average rental rate for buildings, where flexible workspaces are located

** Average rental rate for unassigned and assigned desk

Apart from rental income, flexible workspace operators make profit from additional services – leasing meeting rooms, organizing events, etc. Additional income generally amounts to 10 - 40% of total income.

Flexible workspace supply, Moscow, 2019-2020



DEVELOPMENT FORECAST

In 2018 the market showed 40% growth. In 2019-2020, we expect the growth to remain at the similar level.

In 2019, the supply will increase mostly due to opening of several large flexible spaces (WeWork, Work Station, Meeting Point and others).

Taking into account the current growth rate of flexible workspaces and the size of the unsaturated market, this model has potential for further development.

In the short-term future we expect:

- A rapid increase in the number of operators and the entry of new international players resulting in considerable growth in competition.
- Large corporations to show more interest in flexible workspaces;
- Chain operators to dominate the market;

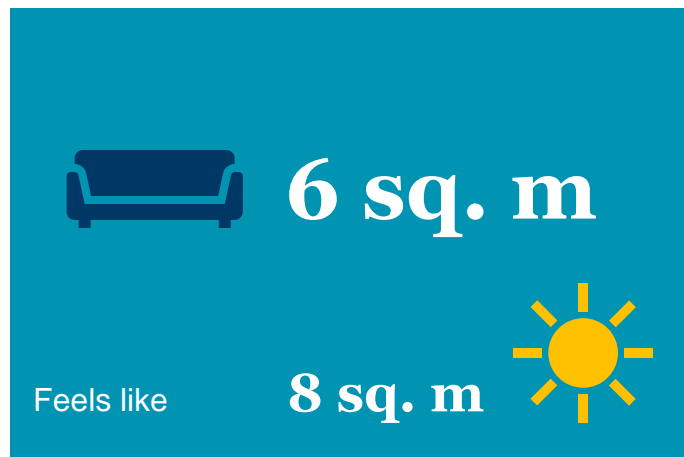
“Chain business models are always ahead of non-chain operators because they are able to distribute costs between (marketing, administration and hosting new clients, etc.). Moreover, being able to redistribute costs and revenue between sites, chains will be more resilient to fluctuations and changes in the market. Small, independent co-working spaces are able to compete with chains, however they will be less efficient and more exposed to the risks”.

Evgeniy Ovchinnikov,
Director, Workki

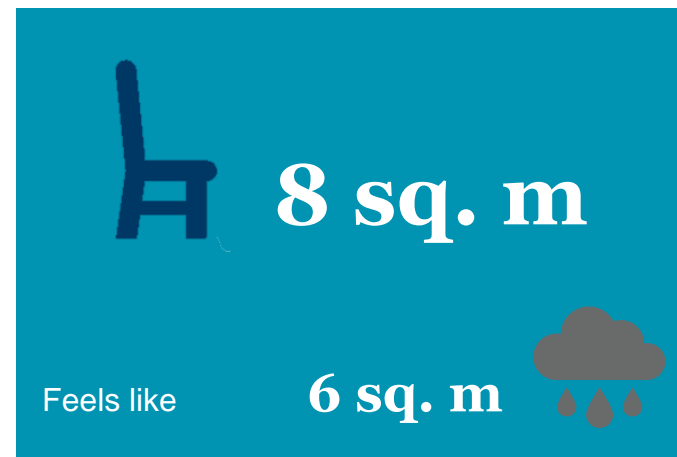
SPACE REQUIREMENT FOR ONE EMPLOYEE

Flexible workspaces advertise comfort at their core and convert real estate into service.

FLEXIBLE WORKSPACE



TRADITIONAL OFFICE



Typically, a single workplace in a flexible workspace make up **6 sq. m**, including common areas. In comparison, the norm in a traditional office is **8-10 sq. m**. Flexible working spaces use space more efficiently – thereby allowing them to charge higher prices per sq. m than traditional offices.

At the same time, despite having in fact less space, users generally feel like they have more space than they would in a standard office. This is thanks to the common areas, the working environment and flexible working hours meaning not all workers are in the office at the same time.

KEY CONCLUSIONS

Transition of real estate into service provision

- At the same time as entering into a long-term lease commitment, the operator provides the end user with a short-term service.

Development of flexible workspaces stimulates further demand

- Given the growing availability of flexible workspaces, start-ups & entrepreneurs have an additional incentive to open and develop their businesses.

The demand for flexible workspaces is high - the market is far from saturated

- There is huge potential for development – the flexible workspace supply will more than double by 2020.

There is no single business model

- Currently the classic long-term lease agreement between operator and landlord is the most popular model. However, flexible workspace operators are constantly experimenting with different models and attempting to work with landlords on a partnership basis.

Appendix

WHAT IS FLEXIBLE WORKSPACE?

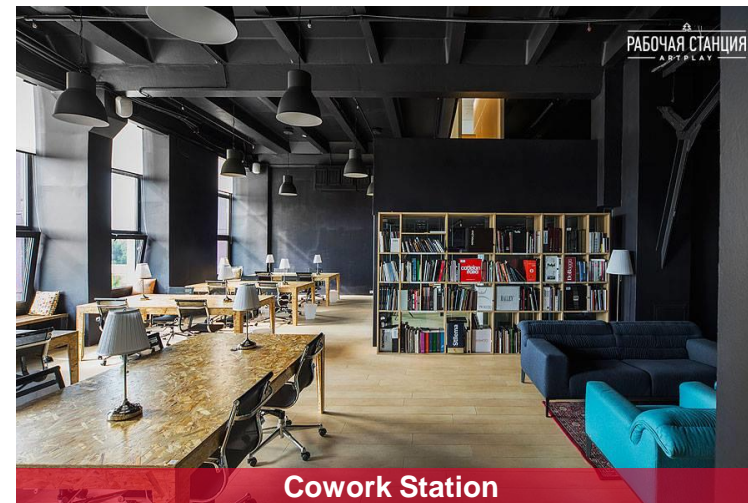
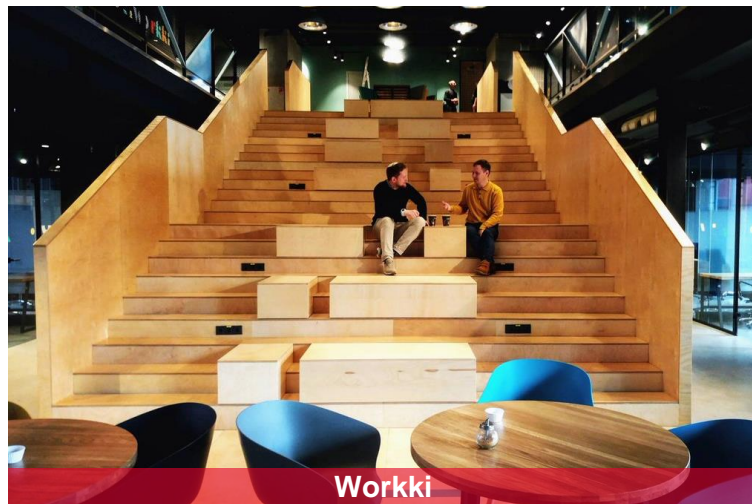
Definition, types of flexible space

WHAT IS A FLEXIBLE WORKSPACE?

Flexible workspace is a broad term that covers all types of **serviced** offices with equipped workstations, that can be leased short-term by one person or a team.

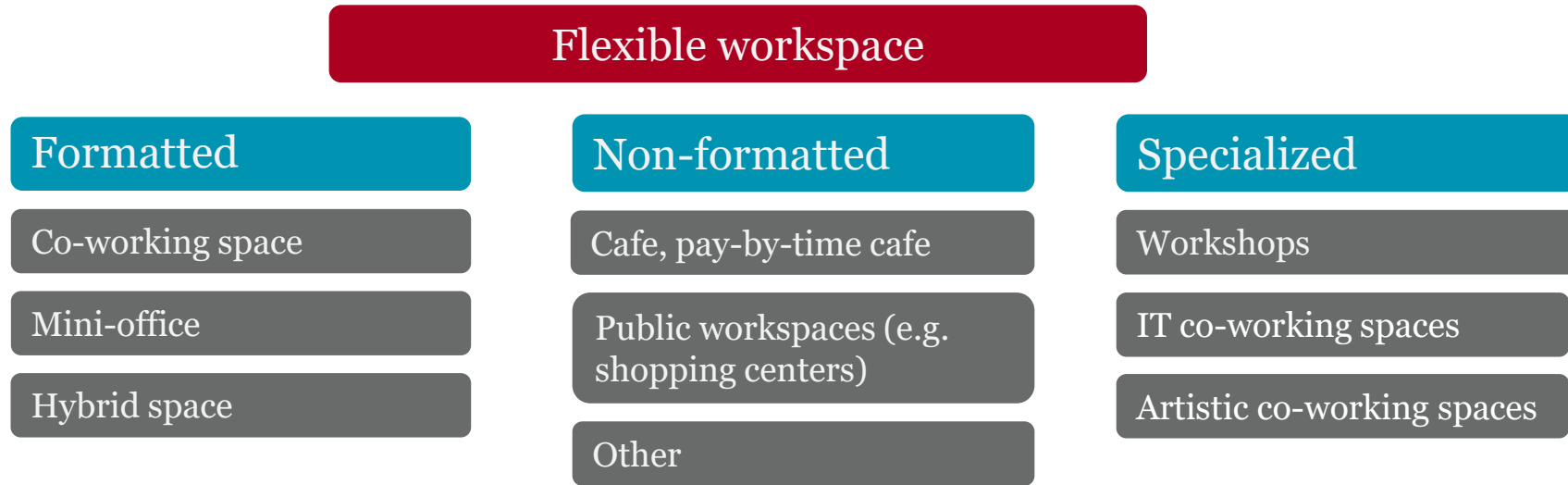
Flexibility means:

- **Possibility of a short-term lease** (from 1 hour to several months);
- **Availability of different formats** (different types of workstations are available – hot desking, assigned desks, mini-offices);
- **Opportunity to choose any number of places** (from a single workstation in a co-working area, to several mini-offices combined with additional co-working desks, with an option of further expansion or reduction down the line).



THE DIFFERENT TYPES OF FLEXIBLE WORKSPACE

There is no common classification for flexible workspaces but it can be broadly divided along the following lines:



The main difference between formatted and non-formatted workspaces is the existence in formatted spaces of dedicated offices with **equipped workplaces**. By comparison, non-formatted workspaces offer this as an additional expense and may have other activities happening at the same time.

Specialized workspaces are focused solely on one specific type of activity. Alternatively, formatted and non-formatted spaces can host people from a range of different industries.

Flexible workspaces can exist either as part of larger chains or as independent entities.

FLEXIBLE WORKSPACE - SERVICES

Formatted flexible workspaces provide the following required services:

- Essential office equipment (desk and storage)
- Common areas & kitchen
- Cleaning
- Wi-fi
- Meeting rooms
- Reception services
- Telephone & printing
- Fully equipped conference halls
- 24/7 access & secure premises

Some spaces may offer additional services. For example, Cowork Station Plaza have a capsule hotel attached and Tablica hybrid space boasts a garden rooftop with bar.



Tablica



Cowork Station

VIRTUAL OFFICE

Flexible workspaces may also provide this key service

Some flexible workspaces provide residents with virtual office services, which allow companies to have all necessary services without the physical presence in the office.

A Virtual office includes:

- Legal address (if necessary);
- Secretarial services (telephone, fax, correspondence distribution, incoming call processing);
- A physical co-working style of office for visitors, clients and meetings;
- A fixed number of hours in meeting rooms.



TENANTS

The target audience depends on the location and pricing policy of flexible workspaces. There are several types of primary users:

1. Young professionals (mostly from IT and consulting), start-ups and small teams of 5-10 people. This is the largest group.
2. International companies, branch offices of foreign and Russian regional companies.
3. Corporate clients who need a temporary office (e.g. during office relocation, staff expansion or for team projects). Currently, the proportion of these clients is still small, but demand is gradually increasing.
4. Freelancers and remote employees make up the smallest percentage of users.

“In 2018, the main majority of demand for flexible workspaces comes from small teams of well-educated young people who are engaged in high-margin business”.

**Pavel Fedorov,
Managing Partner, TheKey**

Appendix

BUSINESS MODELS

DIFFERENT BUSINESS MODELS

Model 1. Leasing premises

- Operator of a flexible workspace leases a big office block, makes the initial capital investment and pays operational expenses, and then leases small blocks or workplaces short-term to the end user.

Model 2. Purchasing premises

- Operator owns the premises, covers capital and operational expenses and leases small blocks or workplaces short-term to the end user.

Model 3. Partnership with a landlord

- Operator leases a space at a discounted rental rate. Landlord/investor covers capital expenses (sometimes split between landlord and operator). Operator is in charge of operational management. Income is shared between landlord and operator.

Model 4. Operator's model

- Landlord provides operator with a fitted-out premises with equipment and furniture. Operator is in charge of operational management and receives a fee from landlord.

THE TRANSFORMATION OF REAL ESTATE INTO A SERVICE PROVIDER

In Russia, the *Leasing* model is the most common: it is the most easily accessible and involves the least risk for landlords. This normally takes the form of long-term lease agreements. Conversely, the risk is significant for operators given the large initial capital investment and long-term commitment to the landlord, at the same time as short term contracts with end-users. The operator must balance the constant risk of having insufficient occupancy rates to cover expenses.

Operator's or partnership models are more preferable for operators as they allow them to split the risks with a landlord. If the flexible workspace is successful, both sides win and the landlord gets higher income from the partnership/operator's model than from simply leasing the space. However, due to recent significant growth in demand in the office market, landlords are unlikely to compromise and accept such risk.

*“The legal relationship between co-working operator and developer is based on a **lease** agreement (through a specific pricing policy). The landlord needs to be confident that the tenant will stay for the long term. The tenant also needs to be sure that he won't be discarded for another tenant willing to pay more.*

*The legal relationship between co-working space operator and resident is a **service** contract. In a service contract, either side may withdraw from this agreement at any time. An operator can discard a resident, a resident can say good bye to the leaser and move to another location. Thus, the co-working operator shoulders the risks of resident turnover”.*

**Konstantine Kouzine,
Partner, Baker & McKenzie**

WORKING IN A FLEXIBLE WORKSPACE: A RESIDENT'S PERSPECTIVE

Advantages

- No need for expensive equipment/infrastructure expenditure;
- Opportunity to lease small block/workplace in a class A or B office building with all services included;
- Possibility of a flexible short-term lease and renting additional workplaces if the number of employees increases;
- Networking opportunities;
- Desirable and trendy working environment;
- Opportunity to take part in events and workshops.

Disadvantages

- Noisy and potentially distracting environment;
- Questions over confidentiality and security;
- Less prestigious and presentable than a traditional office – especially when entertaining clients or partners
- Higher rental rate compared to a traditional office.

“There are confidential clients and confidential files. In my opinion, the idea that these files can be seen by someone else or viewed from a computer screen of a neighbor brings to mind multimillion-dollar lawsuits and loss of business”.

LEASING SPACE TO A CO-WORKING OPERATOR: A LANDLORD'S PERSPECTIVE

Advantages

- Improvements to the building's infrastructure – the flexible workspace format makes a building more attractive both for new tenants and for existing companies;
- Decrease in building's vacancy rate;
- Quality development of space by the operator;
- Increase in building's popularity due to different events organized in the premises;
- No need for parking spaces for non-corporate residents.

Disadvantages

- Risk that users of the flexible workspace won't be compatible with the main residents of the office building.

THE FLEXIBLE WORKSPACE: THE KEY TO SUCCESS

LOCATION

- A flexible workspace should be located within walking distance of the metro (not more than 10 minutes) or in areas of high footfall of target audience (cultural, art or business clusters).

SPACE DISTRIBUTION

- The most effective area of a flexible workspace is 1000 sq. m or more – with a combination of co-working areas, mini-offices and common areas. Mini-offices are in the highest demand due to the Russian mentality of privacy – people want to work in their ‘own’ separate space. However, co-working zones are also needed in order to stay in-line with the concept and atmosphere of a hybrid space.
- Smaller spaces are only worth developing if they can complement the existing infrastructure – e.g. in a hotel, cafe or restaurant.

OCCUPANCY RATE

- Depending on the model, occupancy rates should be 70% or more to break-even.

CHAIN DEVELOPMENT

- Developing a chain of flexible workspaces optimizes efficiency due to economies of scale.

“Occupancy rates should not be less than 70%”.

**Tatyana Sharaeva,
Managing partner, Meeting Point**

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About the company

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