



RESEARCH



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MELBOURNE'S COWORKING CULTURE

RESEARCH INSIGHT

JULY 2016

THE GROWTH AND DRIVERS BEHIND MELBOURNE'S COWORKING INDUSTRY

KEY FINDINGS

Australia has recorded the **highest growth of coworking spaces** in the world (per capita).

61% of coworking providers are planning to expand their operations in 2016.

Melbourne is the 33rd most innovative city in the world.

The participation rate of freelancers and **entrepreneurs in Melbourne is sitting at 12%.**

Venture capital funding in Victoria increased 64% from 2014 to 2015.

Freelancers will make up 40% of the workforce by 2020.

The 55+ age bracket make up the fastest growing segment of entrepreneurship in Australia.

Millennials will make up 50% of the global workforce by 2020.



KIMBERLEY PATERSON
Senior Analyst – VIC Research

Follow at @patersonkimberl

INTRODUCTION

The world is changing at a faster pace than ever before. Coworking, where startups, freelancers, entrepreneurs and small businesses connect with each other through shared workspaces for a membership fee, are attracting attention from large corporates and fast becoming the new required tenant amenity.

Advancements in technology combined with generational and structural economic changes are challenging how the workforce occupies commercial office buildings today. Cellular offices are being phased out in favour of agile, flexible workspaces that are interactive, technology enabled and encourage collaboration.

Coworking has been a rising global trend over the past five years, one widely adopted in Australia which has

recorded the highest growth of coworking spaces in the world (per capita),¹ with Melbourne recording a 43% increase between 2013 to 2015 in the number of small businesses operating,² the coworking industry has grown exponentially. Since the first coworking space opened in Melbourne in 2007, Knight Frank Research has identified more than 100 operators as at Q2 2016, with 750% growth recorded since 2013.

So what is underpinning this exponential growth in coworking across Melbourne and how is coworking influencing corporate workplace designs? In this paper, we explore the concepts of the coworking industry in Melbourne and discuss some of the potential opportunities and impacts on commercial real estate.



Image courtesy of Hub Australia

WHAT IS DRIVING COWORKING?

The expansion of coworking has been fuelled by a number of fundamental changes that are permanently changing where, how and when we work.

Technology

For more than 30 years the concept of flexible working has been evolving, but only recently has the advancement of technology devices, internet connections and cloud computing made working anytime from anywhere possible. Results from the latest Global coworking survey indicate that 61% of coworking providers are planning to expand their operations in 2016, with 87% anticipating their membership base will increase.

Freelancers are increasing

Behind the rapid increase in coworking spaces is the growth of the freelance economy with private equity and crowd funding flowing into local startups. According to the Australian Bureau of

Statistics Australia has approximately one million independent contractors, accounting for 9% of the total workforce. This trend has been adopted more widely in Melbourne with the share of freelancers and entrepreneurs sitting at 12%.³ Venture Capital Funding in Victoria increased by 64% from 2014 to 2015 with \$40 million invested into 25 Victorian headquartered companies, according to Australia Venture Capital Association. Looking ahead, it is estimated freelancers will make up 40% of the workforce by 2020.⁴

Generational changes

Currently entering the workforce, it is estimated Generation Y, also known as Millennials, (born between 1980-2000) will make up 50% of the global workforce by 2020.⁵ Millennials are

driven by vocation, flexibility and work life balance. Their relationship with technology has influenced work styles and communication methods. Their expectations that working environments be interactive and technology enabled is leading to a change in the corporate mindset.

Structural economic changes

Structural economic changes following the most recent economic downturn, has seen more individuals setting up on their own, and this is not exclusively underpinned by just millennials. There is a high prevalence of seniorpreneur activity (Baby Boomers born between 1946-1964) in Australia and they represent the fastest growing segment of entrepreneurship.⁶ Seniorpreneurs are acknowledging their working life will be extended and many have embraced coworking as an alternative to working from home.

The sharing economy

The sharing economy, a key characteristic for millennials, is a growing global phenomenon with renting assets and sharing space becoming economically attractive across a variety of formats. This includes sectors such as transport, with ride sharing services like Uber, accommodation services such as Airbnb, and more recently commercial office platforms such as LiquidSpace allowing any workspace, anywhere, to be rented out on a short term basis. The growth of the creative and technology industry sharing workspace in order to enable production and collaboration through the means of coworking has enabled participation in the sharing economy to become mainstream.



THE SUBMARKETS OF COWORKING ACROSS MELBOURNE

Since the early 1990's Melbourne has prided itself as being well positioned to cultivate innovation for Australia and today is ranked as the 33rd most innovative city in the world (out of 500 cities).⁷

The coworking industry across Melbourne has seen exponential growth since the first space was established nearly a decade ago. This has been underpinned by an increase of freelancers and small businesses (firms with less than four employees) growing by 1,842 companies since 2014, accounting for 87% of all Melbourne businesses.⁸

Excluding serviced office space, Knight Frank Research has identified 152 coworking spaces across Melbourne totalling 58,880 square metres. The number of spaces has increased by 750% over the past three years, with 16 new spaces totalling 13,000 square metres opening in 2016 to date. The average occupancy size is 385 square

metres with 84 operators occupying between the 100-500 square metre size cohort. There are 15 spaces occupying more than 1,000 square metres, with the largest operator - Hub Melbourne, set to occupy 3,900 square metres (from October 2016) at the Mail Exchange Building, 696 Bourke Street in the Melbourne CBD.

Coworking spaces account for 0.8% of total office stock across Melbourne with nearly 90% occupying secondary grade space. Preference differs from traditional office users, with secondary grade and under-utilized stock well suited for this industry from both a cost and fit-out perspective. A large majority of coworking operators across Melbourne, notably in the City Fringe,

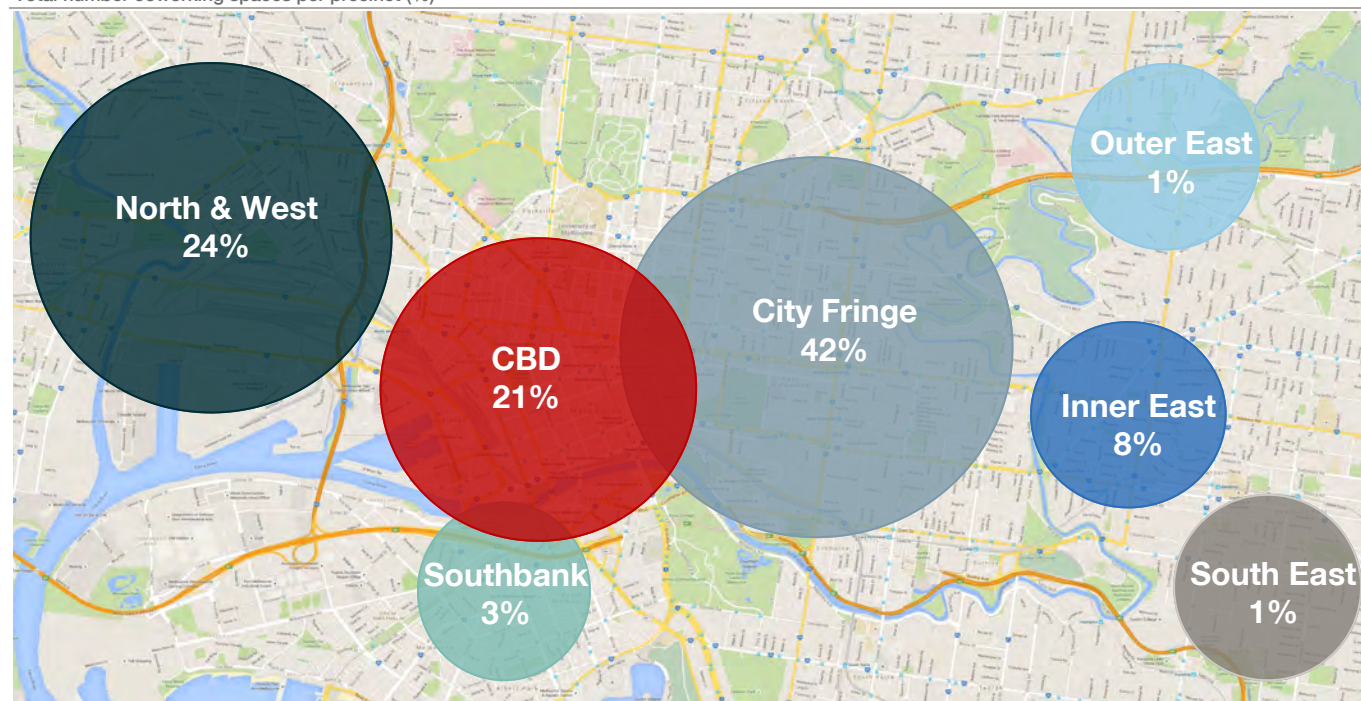
are located in converted warehouses or factories including decommissioned knitting mills, framing factories, woolsheds and heritage listed buildings.

With many operators establishing in lower cost fringe locations, there is evidence of nano-cores (new fashionable zones created in often run down areas) emerging. Areas such as Cremorne, Abbotsford, Collingwood and more recently Footscray, traditionally industrial and manufacturing suburbs, have been revitalized into commercial hubs through a plethora of coworking spaces and the diverse business sectors they attract.

FIGURE 1

The submarkets of coworking in Melbourne

Total number coworking spaces per precinct (%)

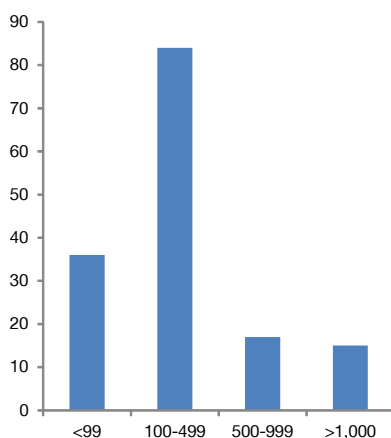


Source: Knight Frank Research

City Fringe

- The City Fringe has the largest volume of space occupied totalling 20,205 square metres, combined with the highest number of operators at 64.
- Coworking spaces account for 2% of total City Fringe office stock.
- The highest concentration of spaces is located in Richmond (excluding Cremorne), accounting for 23% of total coworking spaces in the City Fringe and 10% across the Melbourne market.
- A further 21% of spaces in the City Fringe are located in Collingwood, followed by Cremorne (13%) and St Kilda (9.3%).
- The average occupancy size is 315 square metres, with 35 operators occupying space between the 100 to 500 square metre size cohort.
- There are seven spaces of more than 1,000 square metres, including Launchpad (c.2,500m²), the Commons (1,600m²), Magic Johnston (1,200m²) and Spaces (1,200m²).
- The average rental cost in the City Fringe for a permanent desk space with 24/7 access is \$460 per month.

FIGURE 2
Melbourne coworking space
Number by Size Cohort (000's m²)



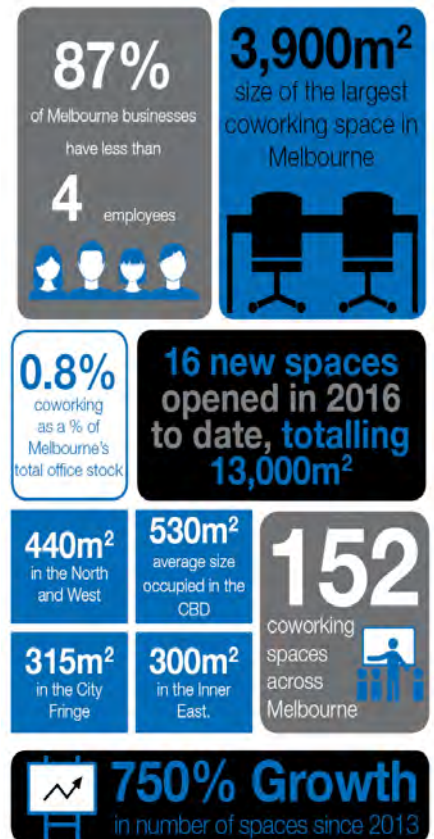
Source: Knight Frank Research

CBD

- The CBD has the second largest volume of space totalling 16,935 square metres with 32 operators.
- Coworking spaces account for 0.4% of total CBD office stock.
- 62% of spaces are located in B-grade and C-grade stock, with 12.5% occupying space in prime grade assets.
- The average area occupied is 530 square metres, with 12 spaces occupying more than 500 square metres.
- The largest coworking spaces include Hub Melbourne (3,900m²) Team Square (2,100m²) and The Cluster (1,600m²).
- The average rental cost for a permanent desk space with 24/7 access in the CBD is \$535 per month.

North & West

- The North & West precinct has the second highest number of coworking sites at 36, accounting for 24% of total spaces across Melbourne.
- Coworking operators occupy 13,305 square metres, representing 6.7% of total office stock in the precinct.
- Brunswick has the highest number of spaces with 11 sites followed by Footscray with eight, and Thornbury/Preston with six.
- Footscray has the largest volume of space totalling 7,790 square metres underpinned by the Dream Factory at 90 Maribyrnong Road, followed by Brunswick with 2,160 square metres.
- The average cost for a permanent desk space with 24/7 access is \$370 per month.
- The average occupancy size is 440 square metres, with 24 operators occupying space between the 100 to 500 square metre size cohort.



Inner East

- There are 12 coworking spaces totalling 3,630 square metres in the Inner East.
- This accounts for 0.7% of total office stock in the precinct.
- The average cost for a permanent desk space with 24/7 access in the Inner East is \$470 per month.
- The average area occupied is 300 square metres, with nearly 60% of spaces located in Prahran.
- The largest coworking spaces include Independent Studios (800m²) Depo8 (460m²) and Gun Alley coworking (400m²).

ONE SIZE DOES NOT FIT ALL

Coworking spaces such as Hub Melbourne, York Butter Factory, Inspire9 and many others across Melbourne, provide shared workspaces for startups, freelancers, entrepreneurs and small businesses.

Workers pay a membership fee to access traditional office facilities and infrastructure when and how they want. This may include a reception desk, mail facilities, meeting rooms with the latest technology, break out areas, printing and high speed internet.

Coworking differs to the serviced office model. According to the Oxford Dictionary, the whole idea of coworking is to bring creative people together and let the ideas collide. Coworking is about a sense of belonging and community. These spaces distinguish themselves by offering social, collaborative, informal, knowledge sharing working environments, promoting interaction, along with educational sessions from market leaders in specific sectors. They are often occupied by those seeking connection and community.

Nevertheless, no one coworking environment is the same in terms of its amenity, services and community.

Creative & community driven

Some providers such as The Commons located in Collingwood, are creative, community driven and accommodate an even mix of startups and established businesses. The Commons provides hot desks, permanent desks and private offices catering for up to eight people. Meetings are held in a repurposed shipping container, there is a meditation lounge, fussball table, arcade machines and a roof terrace.

Entrepreneurialism

Others are focused on entrepreneurialism, catering to more mature stages of business growth such as Launchpad, a multi-site workspace located in Cremorne. Their membership comprises 10% startups, 60% scaleups (entrepreneurs in business for longer than 12 months) and 30% grownups (companies that are completely self-sufficient).

Incubators

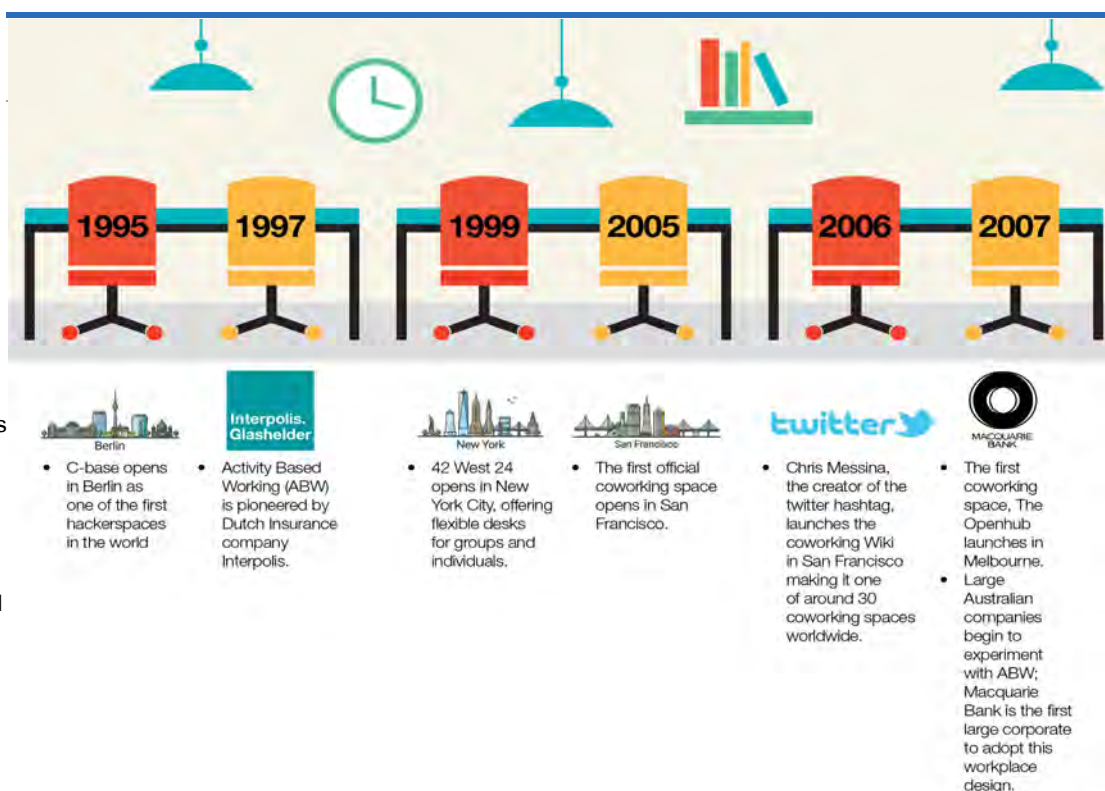
Many spaces combine coworking with startup incubators, accelerators, funding schemes and mentorship support. These spaces generally focus on funding models whereby startups, (usually technology based), are selected through an application or interview process. The York Butter Factory in the Melbourne CBD is an example of this, selecting what startups will be part of their community with their model accommodating 75% post revenue generating businesses.

Growth businesses

Hub Melbourne attracts growth businesses that have an average of two to three staff members with growth potential of up to 10 to 12 employees. Diversity of the space is a key focus for its membership base, with limited technology startups under their roof.

Corporate communities

The NAB Village at 700 Bourke Street, is available to NAB small business customers and community clients. In addition to the marketing benefits, the space creates a sense of community for its customers. The Village Hub provides amenity such as access to meeting rooms, drop in desks and internet services for both its customers and their clients to use, free of charge. Established in February 2014, The Village Hub hosts up to 10 networking and learning events a week and has the largest coworking membership community in Melbourne with over 1,400 members⁹.



WHAT ARE THE BENEFITS?

Amenity

One way coworking spaces differentiate themselves is through the amenity they offer customers. This includes conference and meeting room facilities, reception desk, kitchen amenities, printers and often more unique offerings such as gym facilities, yoga studios, meditation classes, games rooms, free alcoholic beverages, coffee and food. The York Butter Factory for example has a barista grade coffee machine onsite, consuming 30 kilograms of coffee per month for its members and the Commons offers 24/7 free beer. Launchpad has a full size Melbourne W-class tram used as a meeting room and backdrop for staging events, while Hub Melbourne has a gym, a nap room and a relaxation room.

Technology

Access to high speed internet, printers and video conferencing. The plug and play convenience eliminates the distraction of administrative tasks when setting up or running a business.

Flexibility

One of the greatest challenges in starting a business is finding flexible lease terms that allow companies to grow and shrink during this uncertain phase. This is also applicable to established companies that are transitioning, need project space, or are going through periods of uncertainty. Coworking provides a membership structure, allowing business to scale up or down their leasing requirements regardless of the stage their business is at.

Atoms colliding

Working alongside like-minded individuals in a purposeful community can lead to accelerated serendipity. People have the opportunity to knowledge share and collaborate with other creative individuals who they would not normally have exposure to, often connecting them to a new job, opportunity, project or their next team member.

Sense of identity

A recent study by Puzzle Partners compared peoples coworking experiences directly with those working in traditional office environments as well as flexible, activity based environments. People working within coworking and flexible environments typically provided more positive ratings of the environment compared to traditional office environments. Average satisfaction of cellular working environments and flexible working environments was 55% and 78% respectively, while the average satisfaction of coworking was 94%. These people have identified themselves as someone who doesn't fit into a homogenous mainstream corporate office environment and by being part of a coworking environment, they feel empowered and better connected with each other.



Source: Knight Frank Research/DeskMag

HOW IS COWORKING INFLUENCING COMMERCIAL OFFICE SPACE?

The concept of coworking has taken on wider appeal across the Melbourne commercial property market. Fast becoming the new required tenant amenity, corporates are increasingly seeking workplace facilities beyond the traditional office. Property groups such as GPT, Investa, ISPT and DEXUS are providing their own variants of coworking within their assets as tenant amenity and serviced office operators such as Regus are now providing coworking hubs in City Fringe locations.

Work hubs

GPT established Space&Co. on level 10 at Melbourne Central Tower in April 2014 and opened further sites at 530 Collins Street (December 2015) and 580 George St Sydney (February 2016).

Space&Co. was established in response to increased demand from GPT's existing occupier base for more flexible tenant amenity. This was underpinned by a number of factors, including economic uncertainty and a shift in employment towards freelancers and contractors, increasing the difficulty for large corporates to plan their office accommodation requirements. Furthermore, the growth in freelancers and contract workers provided an opportunity to attract a new customer base to GPT and strengthen relationships with key existing customers.

In addition to the traditional arrangements tenants have in their core lease agreements, Space&Co. allows occupiers flexibility on the type and size of space they occupy without any long term commitment. Space&Co. accommodates a diverse range of sectors, offering flexible memberships ranging from day passes to full time fixed desk memberships. More than half of their users are from GPT's existing customer base. The coworking space also gives small companies the opportunity to gain access and affordability into prime buildings with Space&Co. attracting a number of established growing businesses.

Benefits

Amenity: Tenants have additional access to a cafe, meeting rooms, project space, coworking desks and video conference facilities without leaving the building. The creative room at Space&Co. serves as a multifunctional space which can be used as a training facility, auditorium space or a boardroom. The professional amenity offering allows clients and customers to work in an environment that is representative of their brand. The mix of small businesses and established corporates creates an entrepreneurial innovative environment.

Flexibility: GPT is able to cater for changing tenant needs, accommodating temporary leasing requirements as companies grow, downsize, or require flexible expansion space for short term projects. In addition to accommodating a number of tenant project teams, GPT provided Greenland HK with temporary workspace in Space&Co. while they completed their fit-out on level 50 of Melbourne Central Tower.

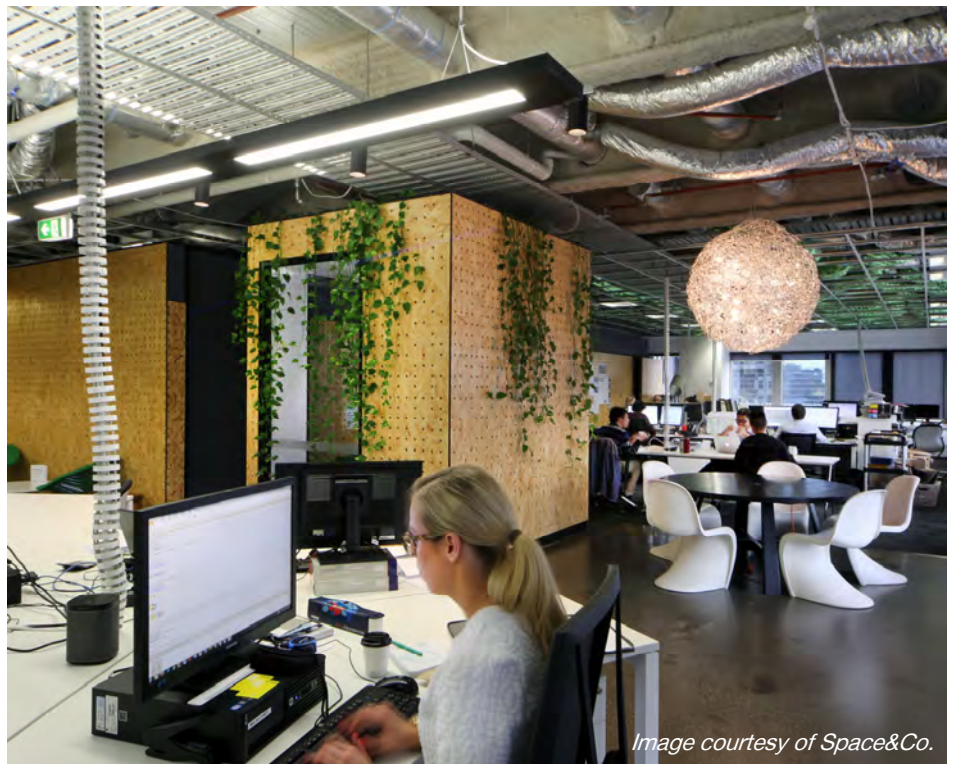


Image courtesy of Space&Co.

Internal collaboration

As demand for coworking increases, corporate work place environments are acknowledging the increased economic value that employees place on collaboration and ideas that evolve from flexible workplace designs.

Corporates have been adopting Activity Based Working (ABW) workplace designs for nearly 20 years. Since that time ABW has been adopted and refined by many corporations throughout Australia including Macquarie Bank (2007), Commonwealth Bank (2010) and more recently in Melbourne with NAB (2013), Medibank (2014), KPMG (2016) and property companies Goodman, GPT, DEXUS and Knight Frank.

ABW typically incorporates four key types of work settings; concentrative, collaborative, interactive and community. It involves the provisions of multiple variations of work point styles, from the traditional work station, to quiet spaces, casual spaces, breakout areas, formal meeting rooms, and open collaborative areas and spaces shared between employees and external clients / service providers.

Benefits

Business: Traditional work practices and processes are re-examined and improved, leading to the business becoming more client facing and responsive.

Internal amenity: Although some larger corporates have gained efficiencies and taken less footprint, some have taken more front of house space including meeting rooms and collaboration hubs, offering employees greater choice of working styles.

Response to business change: Ability to dial up or down the assigned population for immediate capacity, without the need for physical reconfiguration of space.

Productivity: Almost all businesses report higher engagement, productivity and collaboration.

Meeting rooms and project space

DEXUS Property Group established DEXUS Place at 385 Bourke Street on level 14 in December 2015. A DEXUS Place membership is available to tenants within the DEXUS portfolio, offering access to meeting and conference rooms, training rooms, project and event space. By providing additional amenity onsite, this has offered tenants the flexibility to take space as and when required from one hour to 10 years.

Benefits

Reduction in rental costs: Tenants are able to access technology and additional flexible workspace, without investing in an expensive fit-out. By reducing overall footprint, tenants are able to save on rental, fit-out and maintenance costs, outsourcing a large component of their tenancy to DEXUS Place. The business lounges also provide an alternative base to work remotely.

Amenity: DEXUS Place provides tenants off-site access to high quality meeting, training, project rooms, teleconferencing and video conference facilities, boardrooms and internet access without leaving the building.

Serviced offices

Recognizing the aesthetics of coworking, some serviced office operators are evolving their offerings, shifting away from traditional office cubicles and incorporating more collaborative community based environments. Regus for example expanded into the coworking industry in 2015. Responding to the growth of this industry, Regus recently launched and acquired two brands – Kora and Spaces. Located at 580 Church Street in Richmond; Spaces opened in late 2015, aimed towards entrepreneurs and tech-savvy individuals, offering office spaces, meeting rooms and business clubs.

WeWork

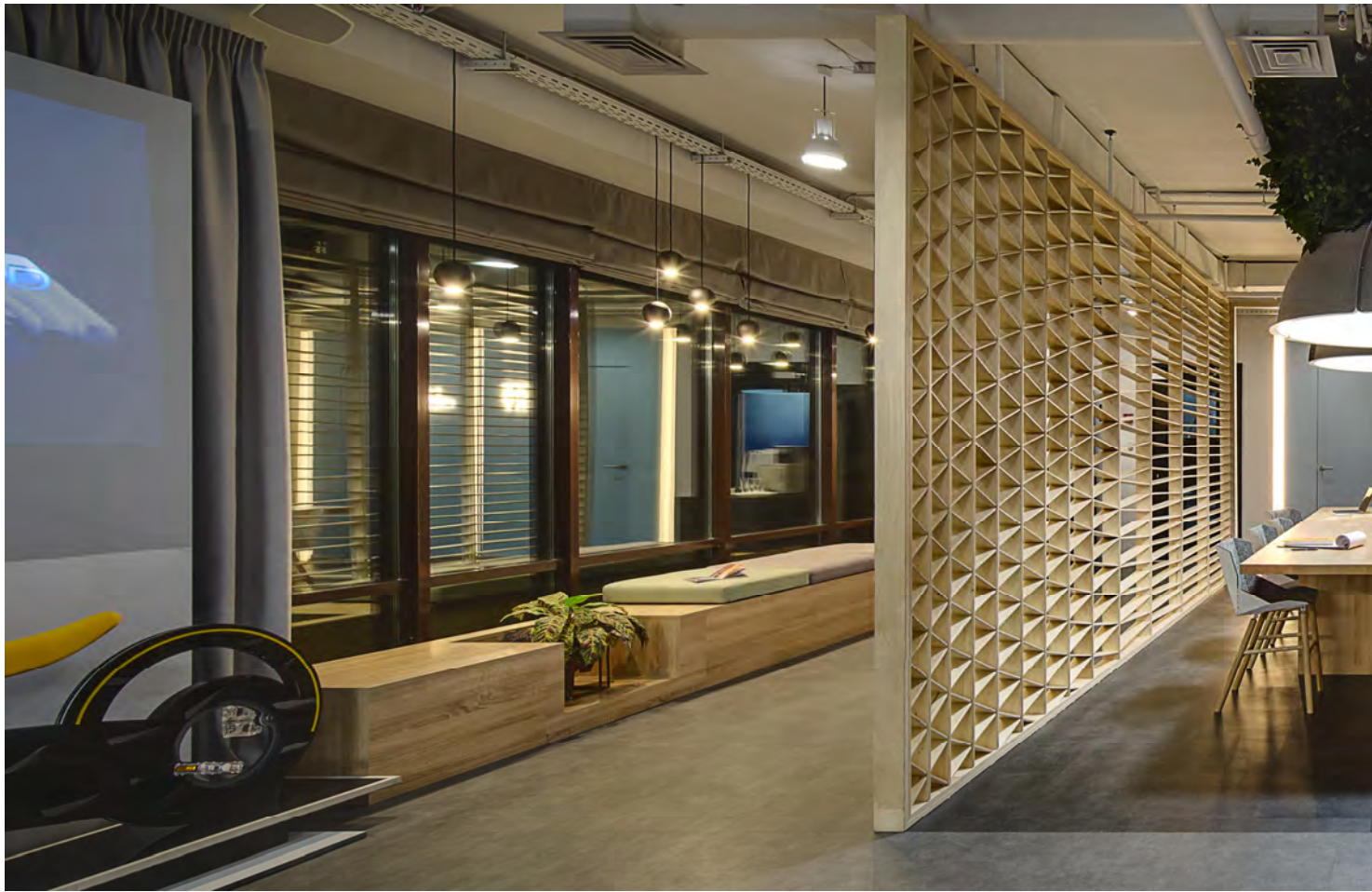
WeWork will open in Sydney in late 2016 and is rumored to launch in Melbourne in 2017, adding a further level of sophistication to the coworking sector. WeWork will offer 500 desks at 5 Martin Place in Sydney's CBD, with members ranging from early stage startups to large multinationals. Private offices range from \$1,150 per month for one person, and up to \$8,250 per month for eight people. A further 1,800 desks will be available at 100 Harris Street, Pyrmont, a converted wool storage facility. WeWork will offer amenity including high speed internet, printing, conference rooms, community managers, weekly events and micro-roasted coffee.

TABLE 1

Top 10 coworking providers by total occupancy in Melbourne

Rank	Provider	Total sqm
1	Hub Melbourne	3,900
2	Team Square	3,100
3	Inspire9	2,900
4	Launchpad	c.2,500
5	ACMI X	2,000
6	The Commons	1,600
7	The Cluster	1,600
8	The Arcade Melbourne	1,230
9	Magic Johnston	1,200
10	Spaces	1,200

Source: Knight Frank Research



HOW WILL COWORKING SHAPE THE FUTURE OF COMMERCIAL OFFICE SPACE?

Corporates and employees are becoming far more agile, acknowledging the benefits of collaborative, innovative and flexible working environments. Nevertheless, this workplace shift has not yet impacted every organization.

Flexibility is at the core of coworking, and one of the main reasons for its success. With advancements in technology enabling people to work anywhere, anytime, there is growing demand from companies and employees to provide more flexible working space, leasing terms, project space and shared space. Landlords who incorporate this into their

workplace design will allow companies that are transitioning, going through periods of growth or uncertainty more flexibility to make real estate decisions that suit the stage of their business.

Should the demand base continue to grow at its current pace, there could be sectors of the market where traditional leasing principles simply no longer apply.

Businesses are increasingly looking to attract and retain the best staff. Workspaces that incorporate some variant of coworking into their workplace design signal to the new generation workforce that they are

open to more flexible forms of working. In the battle for the best and brightest talent, this could prove extremely attractive for tomorrow's workforce and a useful recruitment tool for businesses.

The arrival of WeWork into the Australian market later this year will dramatically increase the market share of the coworking industry and create greater awareness of what different operators can offer. WeWork will encourage more competition and opportunity amongst large established coworking operators in terms of their membership offering. In contrast, smaller, less established coworking



operators that are not large enough to accommodate the churn in vacancies, combined with a fit-out that doesn't match market demand may need to reinvent themselves to compete with WeWork. The spaces that will thrive, will be those that provide added value, situated in a prime location, and offer more than just a hot desk.

Coworking spaces have the potential to create a significant impact, providing startups and small businesses a place to begin operation without the need for a traditional lease and large businesses the opportunity to take flexible amounts of space for short term periods. One view is that these workspace trends will reduce the overall quantum of demand for leased office premises and will also reduce the demand for reactive expansion space, resulting in smaller but more stable tenant requirements. In contrast, the proliferation of

“Shared work has now firmly established itself as the norm for a small but steadily growing percentage of the white collar workforce.”

Matthew Faddy, GPT Group Head of Office and Logistics.

coworking spaces will continue to create new demand for office space through a new industry sector. Furthermore, with coworking spaces incubating startups, greater overall demand for office space could result through the generation of more business ventures.

The next phase of coworking could see corporate occupiers seeking buildings where they can take up a small corporate office on a traditional lease, but only where there is a large coworking space provided within the same building for the majority of employees. This would provide the dual benefit of a corporate home, coupled with the ultimate flexibility of footprint area depending on headcount and workload at any given time, scalable up and down at very short notice. In such a model, the cost of accommodation would follow the headcount per day, rather than years as dictated by the current lease cycle.

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RESEARCH & CONSULTING

Kimberley Paterson

Senior Analyst, Victoria
+61 3 9604 4608
Kimberley.paterson@au.knightfrank.com

Richard Jenkins

Director – VIC Research
+61 3 9604 4713
Richard.jenkins@au.knightfrank.com

Matt Whitby

Group Director
Head of Research and Consultancy
+61 2 9036 6616
Matt.whitby@au.knightfrank.com

VICTORIA

James Templeton

Managing Director, Victoria
+61 3 9604 4724
James.templeton@au.knightfrank.com

OFFICE LEASING

Hamish Sutherland

Senior Director, Head of Division
+61 3 9604 4734
Hamish.sutherland@au.knightfrank.com

Adam Jones

Director – Office Leasing
+61 3 9604 4647
Adam.jones@au.knightfrank.com

James Treloar

Associate Director
+61 3 8545 8619
James.treloar@au.knightfrank.com

GLOBAL CORPORATE SERVICES

Gordon Wyllie

Director - Victoria
+61 3 9604 4666
Gordon.wyllie@au.knightfrank.com

CAPITAL MARKETS

Danny Clark

Head of Commercial Sales, Victoria
+61 3 9604 4686
Danny.clark@au.knightfrank.com

Tim Grant

Director In Charge
Eastern Office, Capital Markets
+61 3 8545 8611
Tim.grant@au.knightfrank.com

VALUATIONS & CONSULTANCY

Michael Schuh

Joint Managing Director – Victoria
+61 3 9604 4617
mschuh@vic.knightfrankval.com.au



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