

VISHAL PANDEY

Flexible Service Office Space

Flexible service office space not only satisfies the need of businesses for greater flexibility during a recession, but also is an early beneficiary during an economic upturn.

A FLEXIBLE SERVICE office (FSO) is one that is fully operational and suitable for immediate occupation. It provides business space on a flexible, short- to medium-term basis to occupiers, especially larger corporations and companies that want to test a new market/location, small and medium enterprises, and startups. The key reason for taking FSO space is either to reduce fixed costs or to meet the needs of project-based work. Its use for overflow space and to provide flexibility is also important; less of a factor is use for startups.

FSO products and services include serviced offices, virtual offices, single-day-stay offices, meeting rooms, and video-conferencing. Among the motivations for individual tenants and companies to take FSOs are the following:

- ▷ instantaneous availability;
- ▷ short-term agreements;
- ▷ lack of complicated leases;
- ▷ flexibility to grow and contract;
- ▷ outsourcing to allow a focus on core business;
- ▷ greater affordability;
- ▷ a pay-as-you-use system; and
- ▷ convenient and high-profile locations.

London is an example of an evolved FSO market where both supply of and demand for FSO space grew at a significant pace, along with that for the traditional office markets.

Between January 2000 and June 2005, the total number of FSO workstations in London nearly doubled, from around 26,000 to 51,000, while the number of occupied FSO workstations increased from 25,000 to 42,800, an increase of about 70 percent.

A conservative estimate suggests that FSO space represents about 0.8 percent of the total traditional office supply in London. The U.K. FSO sector maintained decent occupancy rates despite the economic slowdown of 2001 to 2003. In contrast, the traditional office market saw a significant decline in leasing during the slowdown, followed by a gradual upturn that correlated with the improving economic outlook.

This decline in demand for traditional offices in London occurred for the following reasons:

▷ Overcapacity. The economic downturn led to overcapacity among major corporations. This led to a lag between improved confidence and ensuing increased investment and the return of office demand.

▷ Availability. The U.K., including London, was characterized by large amounts of available space, a significant portion of which was placed on the market by occupiers as sublets—also contributing to the lag between economic recovery and the need for additional space by major occupiers.

▷ Costs. High availability of traditional office space led to a decline in office rents across all major U.K. markets; in the City of London and the West End, rents fell by 30 to 50 percent from the peak of the rental cycle in 2001. The decline in rents and rise in availability may have eroded some of the distinct cost advantages offered by the FSO sector.

▷ Lease reforms. The drive for flexible accommodation and high levels of available space have placed considerable pressure on landlords to provide shorter leases in the traditional office market, with average lease terms declining from 14 years in 1993 to nine years in 2003. This may drive a long-term trend toward shorter leases and may erode the distinct lease length advantage offered by the FSO sector.

As the pendulum in the traditional office market moved progressively toward the tenant, the overall attractiveness of the London FSO sector involved not just flexibility and lower cost, but, more important, service delivery.

Is there a theoretical link between FSOs and traditional offices? Academics suggest that FSO space has evolved out of traditional offices. An oversupply of traditional office space leads to a decline in rents and occupancies, and thus has the ability to erode the cost advantage offered by the FSO sector. Similarly, an oversupply of FSO space results in a marginal decline in workstation pricing structures and lower occupancies. This sometimes results in conversion of some FSO space back to traditional office space.

Thus, the FSO sector is clearly a demand-led product with a high degree of flexibility. **U**

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