Malls and retailers look to co-working startups to fill vacant space

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The recently renovated Staples store at University Ave. and Armoury St. in Toronto, features a 4500 sq foot Staples Studio, a Co-working space with boardrooms, small office rooms and 'phone booths' for private calls. Photographed on Mar 11 2019.

FRED LUM/THE GLOBE AND MAIL

Faced with rising e-commerce competition, retailers and malls are targeting a new type of tenant: office-sharing companies.

For several years, co-working startups – of which New York-based WeWork Cos. is the standard-bearer – have been a growing force in office buildings. Now, they're beginning to pop up in shopping centres and existing stores as landlords look to fill excess space amid a shift in consumer preferences that has led to a wave of faltering retailers, from Sears Canada Inc. to Target Corp.'s Canadian division.

At Upper Canada Mall in Newmarket, Ont., for example, work-sharing startup Lauft recently set up shop at a site next to a former Target outlet. Lauft is now talking to other landlords about moving into their shopping centres.

"We have an eye on being in every shopping mall," said Graham Wong, chief executive and co-founder of Lauft. "We'd like to be as pervasive as Starbucks."

Co-working operators have rapidly moved into office spaces to feed a fast-growing urban appetite for flexible lease terms. Now, work-sharing is branching out to suburban malls and other retail sites as they look to bolster revenues.

The efforts come as vacancy rates at major shopping centres in Canada rose to 10.4 per cent in 2018 from 5.5 per cent five years earlier, according to researcher MSCI. Already in 2019, a spate of retailers has announced more Canadian store closings, including Payless ShoeSource, Gymboree and Home Outfitters.

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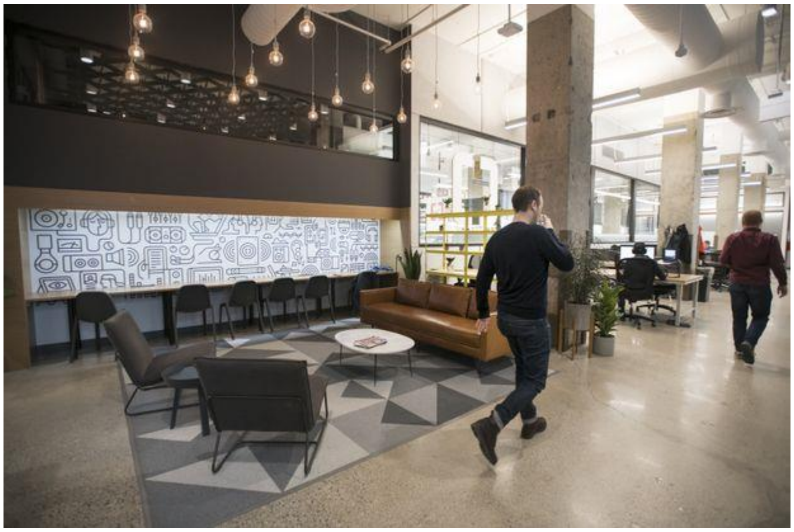
> **ROBERT MARTELLACCI**
> CEO AND FOUNDER OF MINDSHARE WORKSPACE

Susan McGibbon, co-founder of retail consultancy Three Sixty Collective, predicted malls and other mixed-use developments will keep adding more co-working spaces. Ms. McGibbon, whose own offices are in a co-working location in Toronto, said the challenge for co-working operators will be to differentiate their locations from rivals while avoiding "oversaturation" as more competitors crowd the market.

Staples Canada ULC recently launched its first co-working space within one of its downtown Toronto stores that in turn is among its first outlets to be remodelled with the help of designer Joe Mimran. He is putting his modern-classic touch on the



product offerings after having developed the Joe Fresh fashion line at Loblaw Cos. Ltd. and co-founded clothing chain Club Monaco.

David Boone, CEO of Staples Canada, said it gains a co-working edge by offering an array of services such as printing, design and repair resources, guest speakers and a locally-run café. “The landlord response has been tremendous,” he said. Fees for founding members range from $20 for a day pass to $1,999 a month for a private office (and $2,999 for non-members.) It is counting on that revenue to help make up for a 20-per-cent reduction in merchandise space, although it is adding products to its e-commerce site, he said. (In comparison, the annual median gross office rent in that part of downtown Toronto is about $48 per square foot, according to real estate specialist CBRE.) And while privately owned Staples Canada, which he said is profitable, will initially focus on co-working in its urban stores, it will also expand into suburban and even smaller-city outlets, he said.

Meanwhile, mall owners are testing co-working as they race to attract more shoppers in an Amazon age. Oxford Properties Group, owned by Ontario Muncipal Employees Retirement System (OMERS), is piloting various office-sharing initiatives at its sites while expanding its indoor amusement parks, food halls, lounges and restaurants.

Bradley Jones, head of retail at Oxford, said the rash of store closings provides Oxford with “an opportunity to look at our business differently." Co-working is still new, but so far the results are encouraging, bringing more people to the mall who then shop and eat there, he said.

Oxford leases to WeWork in downtown office buildings in Toronto, Boston and Berlin, catering to urban workers. In contrast, Lauft at Oxford’s Upper Canada Mall, which saw both its Target and Sears stores close, is in the suburbs. “Will a model that is an urban model work in the suburbs?” Mr. Jones asked. “We don’t know yet.”

Co-working isn’t a financial slam dunk. Mall landlords generally collect less rent from work-sharing operators – and sign short-term leases – compared with arrangements with regular retailers, betting co-working space will generate more traffic to the mall, industry insiders said.

“We’re a magnet tenant,” said Robert Martellacci, CEO and founder of MindShare Workspace, a co-working operator at Erin Mills Town Centre in Mississauga. “It’s a win-win situation.”

Mr. Martellacci said his lease provides for a lower rent than other retailers at Erin Mills, which also had Target and Sears stores.

Lauft CEO Mr. Wong said it pays rent based on a shared-revenue model rather than a flat fee. Oxford’s Mr. Jones acknowledged the rent is structured differently and can come out to less than what regular retailers pay. As well, Lauft has a one-year lease compared with five- or 10-year terms for other mall merchants, he said.

But even category leader WeWork's expansion faces uncertainties. Toronto-based HBC, which announced in late 2017 it would lease the top floors of its downtown Toronto and Vancouver stores to WeWork, has yet to finalize a Vancouver plan with the startup, HBC CEO Helena Foulkes said in a December interview.

Still, at its Toronto Queen Street West flagship store, Hudson's Bay already has closed its top two floors to make way for WeWork. "From a financial perspective, the financial returns that we'll get from those two floors will be higher than what we were generating," Ms. Foulkes said.