



The Evolution of Real Estate Finance: Exploring the Rise of Co-working Spaces in Indian tier 2 cities

Nysa Sabharwal,
Student
Step By Step

Abstract

This report delves into the dynamic landscape of real estate finance amidst the rise of co-working spaces in Indian tier-2 cities. The research addresses key challenges and opportunities presented by this evolving trend, focusing on adaptability, regulatory hurdles, and long-term implications. Through an explanatory research design and qualitative analysis, the study assesses the compatibility of traditional financing models with the unique demands of co-working spaces, explores regulatory complexities faced by operators, and analyses the transformative impact of co-working trends on urban development. Findings underscore the need for flexible financing structures, regulatory agility, and strategic planning to harness the potential of co-working spaces for sustainable economic growth and community development in tier-2 cities. This research offers valuable insights for developers, investors, and policymakers navigating the evolving dynamics of the commercial real estate sector.

1. Introduction

The main purpose of this research is to evaluate Real Estate Finance and explore the rise of co-working spaces in Indian tier-2 cities. In this research, the researcher elaborated a short description of research problems and then, with the help of secondary data collection, the researcher tried to achieve different objectives. In the findings sections how objectives were achieved was discussed.

2. Research Background

Recently, co-working spaces have revolutionised the commercial real estate scene in India, catering to evolving work dynamics. This kind of shifting is encouraged by the changing work cultures, and enhances flexibility and collaborations departing from traditional office setups (Bergeb-al-Mirabent, 2021). The trend is fuelled by thriving start up ecosystems that offer cost-effective solutions and align with government entrepreneurship initiatives. Legal frameworks such as the Real Estate Regulation and Development Act, 2016 (RERA) mainly ensure compliance while co-working addresses urbanisation challenges by reducing commute needs (Linkedin.com,

2023). Despite the challenge of pandemics, co-working adapts to hybrid models. It provides landlords with stable incomes and offers real estate agents new avenues. Tier 2 cities emerge as promising Commercial Real Estate (CRE) destinations driven by affordability and infrastructure growth (Linkedin.com, 2023). Generally, prospect innovation reshapes the sector that promises a bright future for co-working space amidst demand growth and Tier 2 city opportunities.

3. Research problems and rationale

The research explored the evolution of real estate finance amongst the rise of co-working space in India's tier 2 cities that face key challenges such as lack of privacy, limited amenities, community building and networking, etc (Goldman and Narayan, 2021). Some co-working spaces may need more essential amenities, for example-internet connectivity and meeting room availability.

The research on the evolution of real estate finance and the rise of co-working spaces in Indian Tier 2 cities holds significant importance for different reasons. In 2021, the smartworks co-working operators in India offered 70000 seats across 9 cities in India. It indicates most organisations adopt a hybrid work model that has propelled the growth of co-working spaces in India (Statista.com, 2023). Moreover, in Q1 2023, Co-working spaces represented a notable 27% share of net absorption in the top seven cities, up from 14% in Q1 2019 (Financialexpress.com, 2023). It also highlights the increasing relevance in commercial real estate landscapes. Similarly, the emergence of Tier 2 cities as a new growth engine in the real estate sector driven by different factors, as- improved infrastructure and rapid urbanisation, presents different investment opportunities. Therefore, the research sheds light on understanding the dynamic of real estate financing, mainly for developers, investors, and policymakers to capitalise on the potential growth and navigate the regulatory framework.

The research highlights the issues and provides a solution regarding implementing a reservation system in advance that can help ensure fair access. The researcher analysed the effectiveness of traditional real estate financing models in accommodating the unique dynamics of co-working space (Zukin, 2020). Additionally, it helped to understand the regulatory landscape and compliance issues that are mainly specific to co-working operations in Tier 2 cities which is crucial (Jonek-Kowalska and Wolniak, 2022). This research also evaluated the long-term implication of co-working trends on the overall real estate market dynamics and urban development patterns in Tier 2 cities is necessary for understanding and strategic planning.

4. Aim and Objectives

The research aims to evaluate Real Estate Finance and also explore the Rise of Co-working Spaces in Indian tier-2 cities

Objectives

- To assess and adaptability of traditional real estate financing models to the dynamic of co-working spaces in Indian Tier 2 Cities.
- To investigate the regulatory landscape and challenges faced by the co-working operators in Tier 2 cities.
- To analyse the long-term effects of co-working trends in real estate market dynamics and urban development patterns in tier 2 cities.

5. Literature review

5.1 Adaptability of traditional real estate financing models to the dynamic of co-working spaces in Indian Tier 2 Cities

The rise of co-working spaces has transformed the dynamics of the modern workforce driven by various socio-economic factors. Muthukannan *et al.* (2020) said that urbanisation trends have led to the resurgence of city living that encourages a culture of shared spaces and resources. As people migrate to urban centres, concepts such as communal living have gained traction that lay the groundwork for the co-working movement (Zukin, 2020). Technological advancements have revolutionised work, liberating employees from fixed office space. The advent of cloud computing and remote collaboration tools has enabled individuals to work from anywhere to reduce the necessity for traditional office set-up. This flexibility aligns with the changing attitudes towards employment marked by a departure from the job-for-life pattern. As per Kumar *et al.* (2021), modern workers prioritise autonomy and flexibility and opt for freelance over traditional corporate careers. The evolution of the work environment has spurred the demand for co-working spaces that balance isolation and noise found in alternative work settings. Co-working also provides a conducive environment for small businesses, encouraging collaboration and networking opportunities (Goldman and Narayan, 2021). Large corporations have recognised the benefits of co-working that encourage these spaces to attract top talent and promote innovation.

In terms of its impact on real estate, coworking has reshaped the commercial property market in multifaceted ways, said Vinod *et al.* (2021). Vacant properties have found new life as co-working hubs that mainly contribute to reducing vacancy rates and revitalising commercial centres. Financial institutions view co-working spaces as stable investments due to diversified bases that mitigate the risks of traditional single-tenant leases (Gurbaxani *et al.* 2021). Moreover, co-working has presented opportunities for real estate agents and landlords to capitalise on the trend; it also poses challenges in regulatory compliance and leasing agreements. As co-working leasing laws continue to evolve, stakeholders must navigate legal complexities to ensure the success and sustainability of these spaces.

5.2 Investigation of the regulatory landscape and challenges Faced the co-working operators

The emergence of co-working space represents a paradigm shift in the corporate sector that offers a collaborative work environment conducive to innovation and growth. Apart from the benefits, some different risks and challenges warrant attention. According to, Mukhopadhyay *et al.* (2020), the nature of the global operating landscape is mainly characterised by technological disruptions and uncertainty. That underscores the importance for businesses to remain agile and adaptable. Co-working spaces mainly address this demand for flexibility to provide proper solutions that optimise capital utilisation and reduce fixed investment to provide solutions that optimise capital utilisation and reduced fixed investment. Shaban *et al.* (2020), said that the significant challenges to the co-working industry encourage uncertainties for landlords and investors. Remote work is becoming the norm, and the demand for physical office spaces has dwindled, leading to decreased occupancy rates and profitability (Jonek-Kowalska *et al.* 2022). Economic downturns are expected to persist until the pandemic,

particularly in densely populated countries such as India, where concerns regarding virus transmission remain high.

Similarly, Abusaada *et al.* (2022), said that legal complexities pose additional complexities for both landlords and tenants in the co-working space sector. While leasing out the workplace offers feasible options for landlords and investors. The demand for physical office space leads to declining occupancy rates and profitability. This economic downturn in the market is expected to persist specifically in populated countries such as India, where concerns regarding virus transmission remain high (Desai, 2020). Legal hurdle poses additional complexities for both landlords and tenants in the co-working space sectors. While leasing out workspace offers feasible options for landlords during economic downturns, stringent due diligence is imperative to mitigate risks associated with misconduct. A clear contractual agreement is essential to safeguard the interests of different parties.

Kaw *et al.* (2020), said that different laws create an impact on the co-working space. For example- Zoning and licensing regulations can facilitate the establishment of co-working spaces. Favourable zoning laws enable smooth operations, while stringent regulations increase startup costs. Similarly, build codes assure safety but may escalate construction expenses. Tax incentives spur growth, but excessive taxation hampers small businesses (Sarkar, 2020). Clear labour laws aid workforce management, and strict regulations inflate operational costs. Government programs offer to hurdle support access that impacts co-working space growth.

5.3 Analyzing the long-term effects of co-working trends in real estate market dynamics

The long-term effects of co-working trends on real estate market dynamics are multifaceted and profound. According to, Ullah *et al.* (2021), co-working has sparked a paradigm shift in the commercial real estate landscape to drive a surge in demand for flexible workspace solutions. This trend reshapes traditional office leasing models, with co-working spaces becoming integral components of corporate portfolios (Kumar *et al.* 2021). As co-working continues to gain prominence, it is expected to further diversity and expand to encompass a broader spectrum of industries and sectors beyond the tech and start-up domains.

The rise of co-working spaces is catalysing urban development and revitalising commercial districts, said by Vinod and Sharma, (2021). Underutilised co-working operators breathe new life into urban areas, encouraging innovation hubs to drive economic growth. It extends to peripheral and secondary markets experiencing increased investment and development activity due to the growing demand for flexible workspaces. Co-working also encourages collaboration, innovation and community-building within the real-estate sector (Gurbaxani and Gupte, 2021). Co-working spaces evolved to offer value-added services and amenities, becoming a workplace and hub for networking, professional development and social interaction. This community-centric approach enhances the overall tenant experience and contributes to tenant retention and satisfaction (Vinod and sharma, 2021). The long-term effects of co-working trends in the real estate market dynamics include increased demand for flexible workspace solutions, urban revitalisation that enhanced experiences and shifts in leasing dynamics (Mukhopadhyay *et al.* 2021). As co-working continues to evolve and innovate, its impact on the real-estate sector is expected to be transformative and shape the future of the workplace and urban environment.

6. Methodology

In this research, the researcher used an explanatory research design. The explanatory design helps the researcher to explain why something occurs when limited information is available. In this research, explanatory research design helps the researcher assess the adaptability of traditional real estate financing models to co-working spaces in Indian Tier 2 cities by providing information about how these models have been applied and their effectiveness in changing work dynamics and market conditions (Pandey and Pandey, 2021).

The inductive approach was also used in this study. The inductive approach helped to start with data and observation, then use data patterns to develop theories. The inductive approach helped investigate the regulatory landscape and challenges co-working operators face in Tier 2 cities by gathering specific observations and data from the field. The detailed analysis of these findings aims to identify patterns, trends and regulatory hurdles unique to the Tier 2 city environment (Newman and Gough, 2020).

Qualitative strategy generates non-numerical data, and it is used to understand people's experiences, attitudes, behaviour and interactions. A qualitative research strategy helps to analyse the long-term effects of co-working trends in real estate market dynamics and urban development patterns in Tier 2 cities by delivering stakeholders' perspectives, behaviours and experiences. This strategy provides valuable information to understand complex societal impacts and future trends (Thomas, 2021). In this study, the researcher used secondary data collection. Most of the data was collected from different authentic sources such as Google Scholar, IEEE Xplore, Government websites and so on. The researcher maintains this study's inclusion and exclusion criteria (Budianto, 2020). The researcher also used thematic analysis, mainly emphasising identifying, analysing and interpreting qualitative data patterns. Based on the different objectives, the researcher developed different themes that help achieve objectives effectively.

7. Findings and analysis

7.1 Adaptability of traditional real estate financing models to the dynamic of co-working space in Indian Tier 2 cities

Traditional real estate financing models face challenges adapting to the dynamic nature of co-working spaces requiring a more flexible financing structure. Co-working spaces operate on shorter-term more adaptive leasing models, mainly compared to traditional long-term that necessitate financing arrangement that accommodates these shorter tenancies and fluctuating income streams (Ullah *et al.* 2021). The shift towards flexible co-working spaces poses challenges to evaluating rental income stability for lenders. It can be understood that traditional leases provide a predictable life long-term income stream. Still, co-working spaces may experience a more frequent turnover of tenants which leads to income volatility (Sarkar and Bardha, 2020).

This volatility requires lenders to reassess their underwriting processes and consider alternative metrics, for example, EBITDA, for alternate tenants' potential to gauge the asset's value (Gurbaxani, 2021). Moreover, the evolving nature of co-working spaces is driving the emergence of a hybrid financing structure that mainly combines the elements of traditional real estate loans with the flexibility of leverage financial models (Desai, 2020). Compared to traditional real estate assets, co-working spaces require working capital expenditure and

operational flexibility. The necessary financing arrangements allow for greater flexibility in cash flow and asset management.

7.2 Investigation of the regulatory landscape and challenges faced by the co-working operators in Tier 2 cities.

Zoning regulations in Tier 2 cities may only sometimes accommodate commercial activities such as co-working spaces. Obtaining the necessary permits and licences can take time and effort due to less-defined zoning laws. Co-working spaces must comply with building regulations and safety standards, varying from city to city (Kaw *et al.* 2020). Taxation policies, including GST (Goods and Services Tax) and property taxes, can vary across states and municipalities. Co-working operators must navigate these complex tax structures that may affect the financial viability of their operations.

Tier 2 cities may need more infrastructure to support large-scale co-working operations (Shaban *et al.* 2020). For example, reliable power supply, adequate internet connectivity and limited transportation options can impact the quality of service provided by the co-working spaces. In Pune, Bangalore, and Jamshedpur, co-working spaces are likely to lead to cost savings in the 20-25% range compared to leasing a traditional space (Commonfloor.com, 2023). Recently, Jaipur got five co-working spaces. Many co-working brands are developing in different cities, for example, Indore, Rajkot, Bhubaneswar, etc. Co-working support for co-working spaces to encourage a sense of community and collaboration among members (Mukhopadhyay *et al.* 2020). Understanding and adapting to local social dynamics and cultural norms in Tier 2 cities may pose challenges for co-working operators seeking to build vibrant communities.

7.3 Analysis of the long-term effects of co-working trends in real estate market dynamics and urban development patterns in tier 2 cities.

The growth of co-working space in Tier 2 cities will diversify real estate offerings beyond traditional office spaces. Developers and investors may repurpose existing buildings and the new properties specifically designed to accommodate co-working operators. Co-working spaces can contribute to urban revitalisation efforts in Tier 2 cities by activating underutilised or vacant properties (Vinod and sharma, 2021). Co-working operators often seek out centrally located buildings with historic significance and help to develop new life into neglected areas and contribute to the overall vibrancy of the urban landscape. The availability of co-working spaces can stimulate economic growth and job creation in Tier 2 cities by providing a supportive environment for startups and small businesses. Co-working spaces encourage innovation, collaboration, entrepreneurship and small businesses (Gurbaxani and Gupte, 2021).

Moreover, the growth of co-working spaces in Tier 2 cities may also invest in infrastructure to support the needs of remote workers. The Co-working space in Tier 2 cities is poised to reshape the real estate market dynamics and urban development patterns in significant ways (Shaban *et al.* 2020). Cities such as Jaipur, Indore, Bhubaneswar, and Kota are experiencing a co-working space driven by the rise of startups, increased demands for flexible workplaces and the adoption of remote work trends (Mukhopadhyay *et al.* 2020). This trend is expected to lead to a more diversified real estate landscape in these cities. Similarly, co-working spaces mainly encourage a culture of innovations and collaborations that attract Tier-2 cities as attractive destinations for businesses and talent. The

long-term effects of co-working trends in Tier 2 cities are likely to be transformative, driving sustainable development and enhancing the quality of life for residents.

8. Conclusion

In conclusion, the research evaluates the importance of understanding and adapting to the evolving dynamics of co-working spaces in Tier 2 cities. Several findings shed light on the impact of this trend. Firstly, traditional real estate financing models face challenges in adapting to the dynamic nature of co-working spaces that require a more flexible financing structure to accommodate shorter-term leases and fluctuating income streams. Secondly, the regulatory landscape and challenges the coworking operators face in Tier 2 cities include zoning regulations and permit acquisition complexities, which are important to ensure operational viability. Thirdly, the long-term effects of co-working trends in real estate, leading to a diversification of real estate, mainly offer economic growth and job creation. Stakeholders in the real estate sector, including developers, investors, and policymakers, must navigate regulatory complexities that embrace flexible financing models. It capitalises on the transformative potential of co-working spaces to drive sustainable development and enhance the quality of life in Tier 2 cities.

As co-working continues to reshape the commercial real estate landscape and urban development patterns, strategic planning and proactive measures will be essential to mitigate the challenges. The research highlights the promising future of co-working in Tier 2 cities for economic growth, innovation and community development. Moreover, the evolving nature of co-working spaces is driving the emergence of a hybrid financing structure that mainly combines the elements of traditional real estate loans with the flexibility of leverage financial models. The growth of co-working spaces in Tier 2 cities may also invest in infrastructure to support the needs of remote workers. The Co-working space in Tier 2 cities is poised to reshape the real estate market dynamics and urban development patterns in significant ways. Clear labour laws aid workforce management, and strict regulations inflate operational costs. Government programs offer to hurdle support access that impacts co-working space growth.



References

- Abusaada, H. and Elshater, A., 2022. Examining similarity indicators in six planned capital cities from Africa and Asia: a qualitative research technique. *City, Territory and Architecture*, 9(1), p.33.
- Available at: <https://www.linkedin.com/pulse/evolution-coworking-spaces-indias-commercial-real-estate-vllp2017-0jxlf/> (Accessed on : 26 February 2024)
- Berbegal-Mirabent, J., 2021. What do we know about co-working spaces? Trends and challenges ahead. *Sustainability*, 13(3), p.1416.
- Budianto, A., 2020. Legal research methodology repositions in research on social science. *International Journal of Criminology and Sociology*, 9(1), pp.1339-1346.
- Commonfloor.com, (2024), *Tier 2 cities and coworking spaces*. <https://www.commonfloor.com/guide/tier-2-cities-and-coworking-spaces-56153> (Accessed on : 26 February 2024)
- Desai, D., 2020. Urban densities and the Covid-19 pandemic: Upending the sustainability myth of global megacities. *ORF Occasional Paper*, 244(4), pp.1-4.
- Dzwigol, H., 2022. Research methodology in management science: Triangulation. *Virtual Economics*, 5(1), pp.78-93.
- Financialexpress.com, (2023), *Explained: What will it take for coworking startups to turn unicorns*. Available at: <https://www.financialexpress.com/business/sme-explained-what-will-it-take-for-coworking-startups-in-india-to-become-unicorns-3207772/> (Accessed on : 26 February 2024)
- Goldman, M. and Narayan, D., 2021. Through the optics of finance: Speculative urbanism and the transformation of markets. *International Journal of Urban and Regional Research*, 45(2), pp.209-231.
- Gurbaxani, A. and Gupte, R., 2021. A study on the impact of COVID-19 on investor behaviour of individuals in a small town in the state of Madhya Pradesh, India. *Australasian Accounting, Business and Finance Journal*, 15(1), pp.70-92.
- Jonek-Kowalska, I. and Wolniak, R., 2022. Sharing economies' initiatives in municipal authorities' perspective: research evidence from Poland in the context of smart cities' development. *Sustainability*, 14(4), p.2064.
- Kaw, J.K., Lee, H. and Wahba, S. eds., 2020. *The hidden wealth of cities: Creating, financing, and managing public spaces*. World Bank Publications.
- Kumar, S., Talasila, V. and Pasumarthy, R., 2021. A novel architecture to identify locations for Real Estate Investment. *International Journal of Information Management*, 56, p.102012.
- Linkedin.com, (2023), *The Evolution of Coworking Spaces in India's Commercial Real Estate*
- Mishra, S.B. and Alok, S., 2022. Handbook of research methodology.
- Mukhopadhyay, P., Zerah, M.H. and Denis, E., 2020. Subaltern urbanization: Indian insights for urban theory. *International Journal of Urban and Regional Research*, 44(4), pp.582-598.
- Muthukannan, P., Tan, B., Gozman, D. and Johnson, L., 2020. The emergence of a fintech ecosystem: A case study of the Vizag Fintech Valley in India. *Information & Management*, 57(8), p.103385.

- Newman, M. and Gough, D., 2020. Systematic reviews in educational research: Methodology, perspectives and application. *Systematic reviews in educational research: Methodology, perspectives and application*, pp.3-22.
- Pandey, P. and Pandey, M.M., 2021. *Research methodology tools and techniques*. Bridge Center.
- Sarkar, A. and Bardhan, R., 2020. Socio-physical liveability through socio-spatiality in low-income resettlement archetypes-A case of slum rehabilitation housing in Mumbai, India. *Cities*, 105, p.102840.
- Shaban, A., Kourtiti, K. and Nijkamp, P., 2020. India's urban system: Sustainability and imbalanced growth of cities. *Sustainability*, 12(7), p.2941.
- Statista.com, (2023), *Leading co-working operators in India as of 2021, by number of seats* available at: <https://www.statista.com/statistics/1333401/india-leading-co-working-operators-by-number-of-seats/> (Accessed on : 26 February 2024)
- Thomas, C.G., 2021. *Research methodology and scientific writing*. Thrissur: Springer.
- Ullah, F., Sepasgozar, S.M., Thaheem, M.J. and Al-Turjman, F., 2021. Barriers to the digitalisation and innovation of Australian Smart Real Estate: A managerial perspective on the technology non-adoption. *Environmental Technology & Innovation*, 22, p.101527.
- Vinod, P.P. and Sharma, D., 2021. COVID-19 impact on the sharing economy post-pandemic. *Australasian Accounting, Business and Finance Journal*, 15(1), pp.37-50.
- Zukin, S., 2020. *The innovation complex: Cities, tech, and the new economy*. Oxford University Press.

