



## **GLOBAL MARKETS REPORT**

### **“WeWork failure”**

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## INTRODUCTION

WeWork, once a celebrated unicorn in the coworking space sector, epitomized the potential and peril of rapid business expansion driven by investor enthusiasm rather than sustainable business practices. Originally valued at \$47 billion at its peak in 2019, WeWork's valuation plummeted to less than \$1 billion by 2023, a stark symbol of its failure to meet operational and financial expectations.

WeWork's ambitious growth was substantially fueled by significant investments from SoftBank, which contributed to its high valuation and the following strategic missteps. The company's failure began to surface publicly around its attempted IPO in 2019, which was abruptly pulled due to concerns over governance, financial sustainability, and the viability of its long-term business model. This was further exacerbated by the leadership style of its CEO, Adam Neumann, whose management decisions came under heavy criticism for lack of fiscal prudence and operational inefficiencies.

A critical error in WeWork's strategy was its aggressive leasing of office spaces on long-term contracts without securing sufficient demand, especially in cities like New York and San Francisco. This over-leverage left the company vulnerable when market conditions shifted, particularly with the advent of COVID-19, which drastically reduced the demand for office spaces as remote work became more prevalent. The financial strain was so acute that WeWork had to undergo significant restructuring, including a debt-equity swap with its lenders to avoid a complete collapse. This move erased \$3 billion of its debt but diminished the equity value for existing stakeholders. Moreover, the company's attempt to pivot to a "space-as-a-service" model, which aimed to offer more flexible workspace solutions, did not generate the expected turnaround.

Despite these efforts, WeWork's tale serves as a cautionary narrative about the dangers of overvaluation based on speculative growth, the importance of sustainable business practices, and the need for robust corporate governance. This story highlights a broader theme in the tech and startup sectors, where the pursuit of rapid expansion often overshadows the foundational principles of business viability and fiscal responsibility.

The downfall of WeWork has resonated beyond its immediate financial implications, casting a long shadow over the global real estate and investment markets. The company's crash forced a reevaluation of valuation practices and investment strategies, particularly within the technology and startup sectors. Investors are now more cautious, scrutinizing the sustainability and scalability of business models more rigorously before committing funds. This shift marks a significant departure from the previous trend where the potential for rapid growth often overshadowed foundational economic viability. Consequently, the WeWork debacle has instilled a more conservative approach to venture capital and private equity investments, prompting investors to demand greater transparency and accountability from their portfolio companies.

Globally, the commercial real estate market has also felt the ripple effects of WeWork's restructuring and downsizing. The firm's massive footprint in major cities worldwide meant that its reduction in office space had a direct impact on real estate dynamics, contributing to increased vacancy rates and pressuring property values. The uncertainty surrounding large coworking space providers has led landlords and property developers to diversify their tenant base and reduce reliance on single, large occupants. Moreover, this situation has accelerated the adoption of more flexible lease terms and increased the availability of 'flex' spaces, which cater to a growing demand from companies seeking shorter, more adaptable occupational commitments in response to an evolving work environment.

## **WeWork STORY UNTIL 2019**

WeWork, the coworking giant that fundamentally reshaped the concept of office spaces, was founded in 2010 by Adam Neumann and Miguel McKelvey in New York City. Their vision was to create spaces that fostered community and collaboration among businesses and entrepreneurs. This idea was born out of their first venture, Green Desk, which emphasized eco-friendly workspaces. The company rapidly expanded its footprint after opening its first location in SoHo, New York, by securing significant funding and exploring innovative business models. WeWork's early growth was marked by rapid expansion both domestically and internationally. By 2011, WeWork launched WeWork Labs, its incubator program to support startups, which emphasized the company's commitment to fostering entrepreneurial communities.

In the years that followed, WeWork continued to attract substantial investment, helping to fuel its expansion. Significant funding rounds in 2012 and 2013 allowed it to spread across major U.S. cities and beyond. By 2014, WeWork had opened its first international location in London and continued to grow its global presence aggressively. WeWork's innovative approach to office spaces, combining flexible leases with vibrant community activities, appealed to a broad spectrum of freelancers, startups, and even large enterprises. By 2016, the company boasted a valuation of \$16 billion, reflecting its rapid ascent within the commercial real estate sector. The same year, WeWork also ventured into the residential space with WeLive, providing flexible living accommodations that complemented its workspaces.

2017 was a particularly pivotal year for WeWork as it continued to expand its global footprint and diversified its offerings. This included the acquisition of large properties like the iconic Lord & Taylor Building on Fifth Avenue and launching initiatives like the WeGrow educational platform and the Rise by We wellness club. Throughout its expansion, WeWork not only reshaped how spaces were utilized but also how they were perceived in terms of their impact on productivity and community building. It prioritized a blend of work, live, and play environments that catered to a modern workforce looking for flexibility and a sense of community.

As WeWork moved towards its peak valuation in 2019, the foundational strategy of aggressive expansion and community-building remained central. However, as would later become evident, the very strategies that facilitated its meteoric rise also sowed the seeds for future challenges. WeWork's story up to this point is a testament to how innovative business models can disrupt traditional industries, yet also highlights the risks associated with rapid growth and high valuations.

## **WeWork BUSINESS MODEL**

WeWork's business model revolutionized the office space industry by leveraging a combination of real estate and technology to offer flexible workspaces that catered to the needs of freelancers, startups, and large corporations alike. This model is often referred to as "space-as-a-service," and it encapsulates the essence of WeWork's strategy: providing not just physical office spaces but a complete ecosystem that supports business growth and networking. Main aspects of WeWork business model that differentiate it from many competitors are:

### 1. Core Offering of Flexible Office Spaces.

At the heart of WeWork's business model lies its flexible office spaces. Unlike traditional office leases that often require long-term commitments (often 10-15 years), WeWork offers terms as short as one month, which appeals to companies of all sizes that seek flexibility. This model allows businesses to expand or reduce their office space based on their current needs without the typical constraints of traditional real estate agreements.

### 2. Diverse Membership Options.

WeWork's offerings are tiered to accommodate different types of workers and companies. Each of these tiers is priced differently, providing flexibility and a variety of options depending on the member's needs. Offerings are:

- Hot Desks: This option allows individuals to occupy any available desk in a common area on a first-come, first-served basis.
- Dedicated Desks: Members get a desk of their own in a shared office.
- Private Offices: Fully enclosed, lockable spaces that can accommodate teams of any size.
- Custom Buildouts: WeWork also offers the option to customize office spaces according to the specific needs of larger clients.

### 3. Value-Added Services.

Beyond just offering space, WeWork attempts to differentiate itself by providing a range of services that add significant value for its occupants:

- Community Events: WeWork hosts numerous events ranging from networking events and workshops to social gatherings, which are designed to foster a sense of community.

- Business Services: Through partnerships with various service providers, WeWork offers its members discounted rates on services such as health insurance, payroll processing, IT support, and more.
- Technology: WeWork provides high-speed internet and has developed proprietary technology platforms that help members manage their space, book conference rooms, and connect with other community members.

#### 4. Global Network.

A key component of WeWork's appeal is its global network of workspaces. Membership at one WeWork location provides access to WeWork's entire global network, which is attractive for businesses that require travel or have multiple locations. This global presence not only allows for seamless working as members travel but also provides businesses with instant access to numerous markets.

#### 5. Real Estate Strategy.

WeWork's approach to real estate is another cornerstone of its business model. Rather than owning properties, WeWork mostly leases them. This has allowed WeWork to expand rapidly without the upfront capital expenditure typically required to buy real estate. However, this strategy also implies significant fixed costs due to long-term leases, which became a financial burden when occupancy rates fluctuate.

#### 6. Community and Brand.

The brand and the community-centric model are integral to WeWork's value proposition. WeWork markets its workspaces not just as places to work, but as environments that enhance productivity and creativity. By curating a community of like-minded professionals and companies, WeWork creates a network effect that becomes a self-reinforcing attraction.

#### 7. Monetization through Density.

WeWork's financial model relies heavily on achieving high density within its locations. By designing spaces that can accommodate many members relative to the square footage, WeWork aims to maximize revenue per square foot. This strategy hinges on maintaining high occupancy rates, which are crucial for the company's profitability.

#### 8. Scalability and Adaptation.

Initially, WeWork's growth strategy focused on aggressive expansion to capture market share quickly. Over time, the company had to adapt its model, scaling back in some areas and focusing on profitability overgrowth. This included divesting non-core ventures and enhancing operational efficiencies.

## CRITICAL POINTS OF THE BUSINESS

Before its crisis, WeWork's business model exhibited several critical aspects and points that contributed to both its rapid growth and subsequent challenges.

### 1. Aggressive Expansion Strategy.

WeWork pursued an aggressive growth strategy, expanding its footprint globally at a rapid pace. This was driven by the pursuit of market dominance in the coworking space sector and aimed at capitalizing on the growing demand for flexible office solutions. While this strategy allowed WeWork to scale its operations and brand presence quickly, it also involved substantial financial risk. The company took on significant debt through long-term leases in prime locations worldwide, betting on continued high demand for shared workspaces which eventually became a financial strain.

### 2. High Operating Costs.

Related to its expansion was WeWork's high operating cost structure. The company leased large properties at premium locations, which required considerable upfront investment to develop into coworking spaces that matched the brand's aesthetic and functional standards. While these investments made the spaces attractive to potential members, they also meant that WeWork carried substantial ongoing costs, particularly in markets where the demand for coworking spaces did not meet expectations.

### 3. Dependency on Continuous Investment.

WeWork's business model was heavily reliant on external funding. The company raised billions in venture capital to support its expansion efforts. This reliance on continuous investor support made the business vulnerable to shifts in investor sentiment and broader market dynamics. As seen in 2019, investor skepticism around the time of its planned IPO highlighted concerns over the company's profitability and long-term sustainability, significantly impacting its valuation and ability to secure further funds.

### 4. Flexible Lease Model vs. Fixed Costs.

A critical tension in WeWork's model was between the flexibility offered to members and the fixed costs of its lease obligations. Members could sign up for short-term memberships or adjust their space needs on relatively short notice, which was a key selling point of the service. However, WeWork's own commitments to landlords were typically fixed on much longer terms. This mismatch exposed the company to risks if it could not maintain high occupancy rates.

### 5. Community Building and Branding.

A significant aspect of WeWork's appeal was its community-centric approach. The company didn't just offer office space; it provided a community for networking, professional development, and social interactions. This focus on creating a vibrant community was successful in attracting a diverse membership base. However, the costs associated with maintaining such an engaging environment were substantial and required constant innovation and management focus to keep the value proposition fresh and appealing.

#### 6. Innovation and Diversification.

WeWork attempted to innovate beyond just providing office space. It ventured into living spaces (WeLive), education (WeGrow), and even fitness (Rise by We). These initiatives were meant to diversify revenue streams and deepen the integration of its community. While these were bold moves, they also stretched the company's focus and resources, and not all were successful or well-integrated into the core business model, leading to criticisms of overreach.

#### 7. Governance and Management Challenges.

Leadership and governance were perhaps the most scrutinized aspects of WeWork ahead of its failed IPO. The company's governance structure, particularly the outsized control held by its CEO and co-founder, Adam Neumann, raised significant concerns among investors and analysts. Issues such as conflict of interest, management practices, and strategic decisions were viewed as red flags that ultimately affected investor confidence and the company's public perception.

## **FINANCIAL CRISIS: REVEALED BUSINESS STRUCTURE AND MANAGEMENT FAILURES**

On August 14th, 2019, the filing of the initial public offering (IPO) left observers and market participants alike astonished. The document revealed the intricate details of WeWork's business structure, which was described as a "UP-C" structure by financial analysts. This structure offered certain advantages to insiders, including Neumann, who were able to minimize their taxes on profits through individual income tax rates. However, public shareholders faced double taxation due to the double taxation loophole. This allowed the holding company to pay taxes on its income, and then on any dividend distributions. The structure also created different share classes, which would give Neumann 20 times as many votes per share as ordinary shareholders.

Moreover, the Neumann family would retain control even in the event of Adam's death, with his wife Rebekah - who had been elevated to co-founder - holding the right to select his successor. This led investors to express concern about the unrestricted control of the founder's family. Secondly, the filing revealed that WeWork had paid Neumann rent on buildings he owned and purchased the trademark to the word "We" from him for \$5.9 million. This suggests that the founder was enriching himself at



the company's expense. Thirdly, investors found the company's financials even more concerning and realized that the company would not be able to produce real profits with its current business strategy. The operating expenses for the company's locations for the six months ending June 30, 2019, increased by twofold compared to the same period in the previous year. This resulted in total expenses of \$2.9 billion, a loss from operations of \$1.4 billion, and a net loss of \$904.7 million for the six months. These figures led to negative profitability ratios (ROTA, ROE, ROS) and demonstrated that, with its current cost structure, WeWork would not be able to generate a profit. Moreover, the company's net interest income of \$470 million, cash balance of \$2.5 billion, total equity deficit of \$2.3 billion, and total liabilities of \$24.6 billion provided investors with a clear indication that the company was overleveraged and would be unable to repay its debt shortly.

Despite the company's precarious financial situation, Neumann persisted in making imprudent investments, including the opening of an elementary school WeGrow in New York, an investment in an indoor wave pool company, and the purchase of a private jet for \$60 million. The final straw was in mid-September when the Wall Street Journal published details of Neumann's in-flight marijuana consumption. It became evident that without significant governance reforms, the IPO would be unsuccessful, which would result in the demise of WeWork, which had only \$2 billion in cash reserves (sufficient for a mere two months of operations). Consequently, on September 24<sup>th</sup> Neumann stepped down as CEO amid scrutiny from WeWork's board members and investors over his leadership - including allegations of self-dealing - and financial problems, after the company delayed its IPO the previous week and reduced its estimated market valuation to \$10 billion from \$47 billion.

In response to the mounting financial pressures, the company sold Neumann's \$60 million private jet, put many WeWork acquisitions up for sale, postponed the IPO indefinitely, closed down WeGrow, and fired thousands of employees. At the same time, the company secured itself multimillion-dollar severance packages. Nevertheless, the widespread concerns about the business model, and Neumann's behavior (including the numerous conflicts of interest), caused the IPO to be delayed and eventually withdrawn. Specifically, on September 30<sup>th</sup> WeWork submitted a request to federal regulators to withdraw its IPO plans, with co-CEOs Artie Minson and Sebastian Gunningham, Neumann's replacements, saying the company wanted to "focus on our core business, the fundamentals of which remain strong."

## **SOFTBANK BAILOUT**

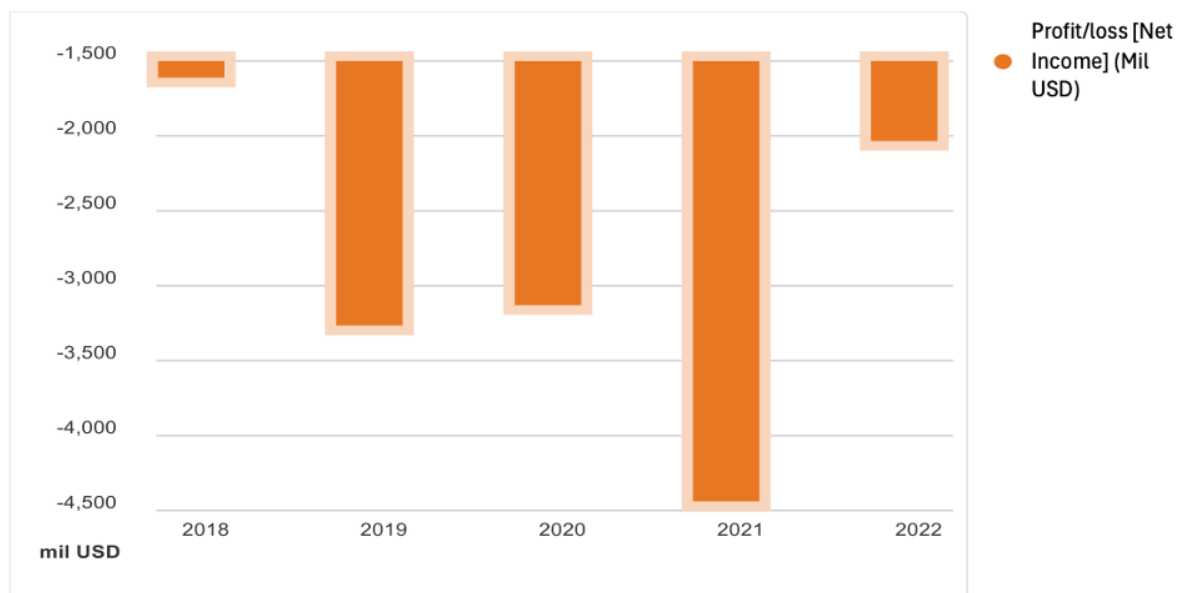
After that, the advisers determined that WeWork required a rapid infusion of approximately \$5 billion in order to maintain its operations. SoftBank, the largest investor in WeWork, once again provided a lifeline to the startup by offering \$5 billion in new debt, purchasing up to \$3 billion worth of stock from existing investors, and injecting \$1.5 billion in new capital. Additionally, Son demanded that Neumann relinquish his chairmanship and transfer his voting rights to the board. To enhance the appeal of the offer, the Japanese conglomerate proposed a credit line to repay a \$500 million bank facility on which Neumann was technically in default, agreed to a \$185 million consulting fee, and indicated that SoftBank could purchase up to \$970 million of Neumann's shares. With just two weeks'

worth of cash remaining, Neumann and WeWork accepted the bailout proposal. The company's valuation of \$8 billion was just over a sixth of the \$47 billion valuation that Son and Neumann had agreed on just 10 months earlier. Even after the rescue, WeWork's financial position was not robust. The company had \$50 billion of lease obligations it had promised to fulfill and even publicly acknowledged that the spectacular failure of its IPO plans could scare off new customers and business partners.

## THE CONSEQUENCES OF PANDEMICS

The loss sustained by WeWork during the 2020 financial year was \$3.2 billion as a direct consequence of the global shutdown of its co-working spaces due to the impact of the Covid-19 pandemic. This represents a narrowing of the losses incurred in the previous year, 2019, which stood at \$3.5 billion (see Figure 1). This narrowing can be attributed to two factors. Firstly, the company's expenditure on capital decreased from \$2.2 billion in 2019 to just \$49 million in 2020. Secondly, the occupancy rates of WeWork's global portfolio declined from 72% at the beginning of 2020 to 47% at the end of the year, a reduction that had an impact on the company's financial performance in the year under review.

Figure 1. Yearly Net Income (Mil USD)



The occupancy rates across WeWork's global portfolio declined from 72% at the beginning of 2020 to 47% at the year's end. However, the company's new CEO, Sandeep Mathrani, a veteran retail real estate executive, was able to improve its financial performance. The company reduced its overhead costs by \$1.1 billion and trimmed \$400 million in operating expenses, which improved its free cash flow by \$1.6 billion. By December 2020, the company had exited 106 underperforming or not-yet-opened locations and negotiated more than 100 lease amendments that collectively added up to an

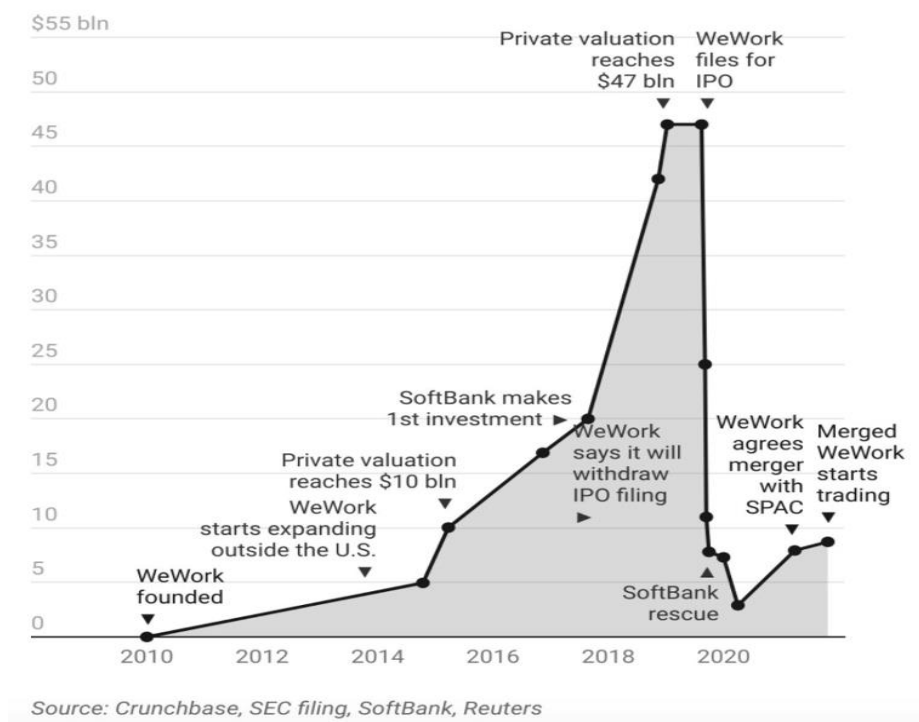
estimated \$4 billion reduction in future lease payments. Additionally, a growing share of WeWork's memberships – 54% compared to 43% last year – was coming from enterprise companies that have 500 or more employees. These companies, which often lease entire floors or buildings, are more stable than individual memberships. In response to the pandemic, WeWork launched several new profitable projects to assist small and medium-sized businesses. It also offered more flexible options to tenants in the UK who wished to split their work between their homes and offices.

Furthermore, WeWork provided £15 million to subsidize rents for struggling SME. The pandemic has fundamentally altered the landscape of work, precipitating a surge in demand for flexible workspace among organizations of all sizes. Despite WeWork's efforts to adapt and offer new solutions to its clients, the company faced a significant challenge due to the discrepancy between its long-term leases and short-term revenues. Indeed, the company had entered the majority of these leases with landlords before the onset of the pandemic when rents were at their highest. However, in 2020, it was anticipated that office rent would be paid at a lower rate, given that there was a lower demand. Newer locations were also less likely to be fully occupied, given that it takes time to fill them with tenants, resulting in a lower total rent than mature locations did. In other words, for its newer locations, WeWork was paying more than it received.

## 2021 IPO

Since then, the recovery from the pandemic has accelerated the rise in demand for flexible workspaces as more workers embraced full remote or hybrid work setups. In such a context, WeWork entered in March 2021 into a \$9 billion merger with BowX Acquisition, a SPAC (special purpose acquisition company). As part of the deal, SoftBank retained a majority stake in the company, but agreed to a one-year lock-up on its shares. A few months later, specifically in May, the Financial Times reported that WeWork's losses were worsening even as the company prepared for its merger with BowX. However, despite ongoing losses (WeWork lost \$2.1bn in the first quarter of the year, which included a \$500m non-cash settlement with Neumann), the deal was finalized on October 20<sup>th</sup>, when the shareholders of BowX Acquisition voted in favor of its transaction with WeWork and the new entity began trading on the New York Stock Exchange under the ticker WE. Thus, on October 21<sup>st</sup> WeWork went public with shares rising 13% by the end of the day to \$11.38, implying a valuation of \$9bn five times less than its initial valuation in 2019. WeWork received \$1.3 billion in cash from its deal with BowX Acquisition, which included money held in the SPAC trust from BowX's IPO, as well as a \$150 million investment from Cushman & Wakefield that acted as a backstop for shareholder redemptions. Investors including Starwood Capital Group, Insight Partners, and BlackRock committed an additional \$800 million through a private investment in public equity. SoftBank provided WeWork with a \$550 million senior secured note, and Adam Neumann retained an 11% stake, although he could not sell shares for nine months.

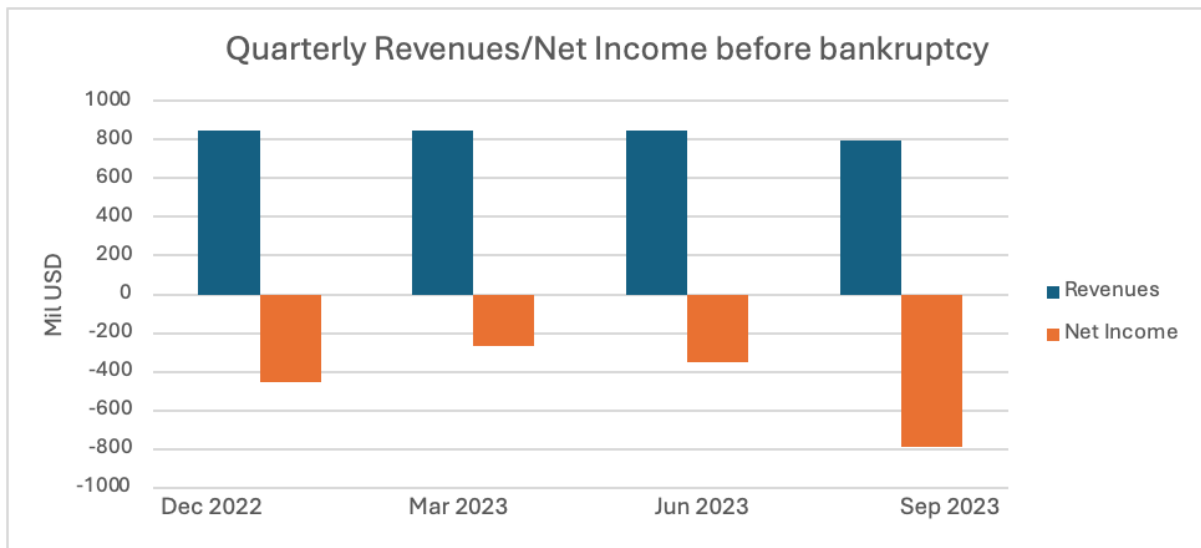
Figure 2. Evolution of WeWork EV over time until October 21<sup>st</sup>, 2021



## WeWork's Rollercoaster Ride: From Recovery to Bankruptcy

Despite the serious financial situation WeWork was in, as evidenced by Figure 2 the company's stock value seemed to be recovering after completing the merger transaction with BowX Acquisition. Then, in August 2022, WeWork announced a milestone achievement, with its offices reaching pre-pandemic occupancy levels of 72%, indicating a rebound from the initial impacts of COVID-19. However, by August 8, 2023, the company's financial problems became apparent as it reported significant losses (see Figure 3) and negative cash flows, casting doubt on its ability to sustain operations. This led to a warning of potential bankruptcy in a Securities and Exchange Commission filing. On September 6, 2023, WeWork unveiled plans to renegotiate most of its leases, opting to exit "unfit and underperforming locations" while redirecting investments into more promising markets as a strategy to cut operating costs and ensure long-term viability. Despite these efforts, on November 6, 2023, WeWork filed for Chapter 11 bankruptcy, resulting in a drastic decline in its stock price to 84 cents per share and a valuation of \$44.5 million. However, it is important to highlight that WeWork's bankruptcy filing is limited to its spaces in the U.S. and Canada, and the company has 777 locations across 39 countries. On November 6, over 400 of its other entities filed for bankruptcy too, including "many individual subsidiaries" it used to run its spaces in other countries, the Wall Street Journal reported.

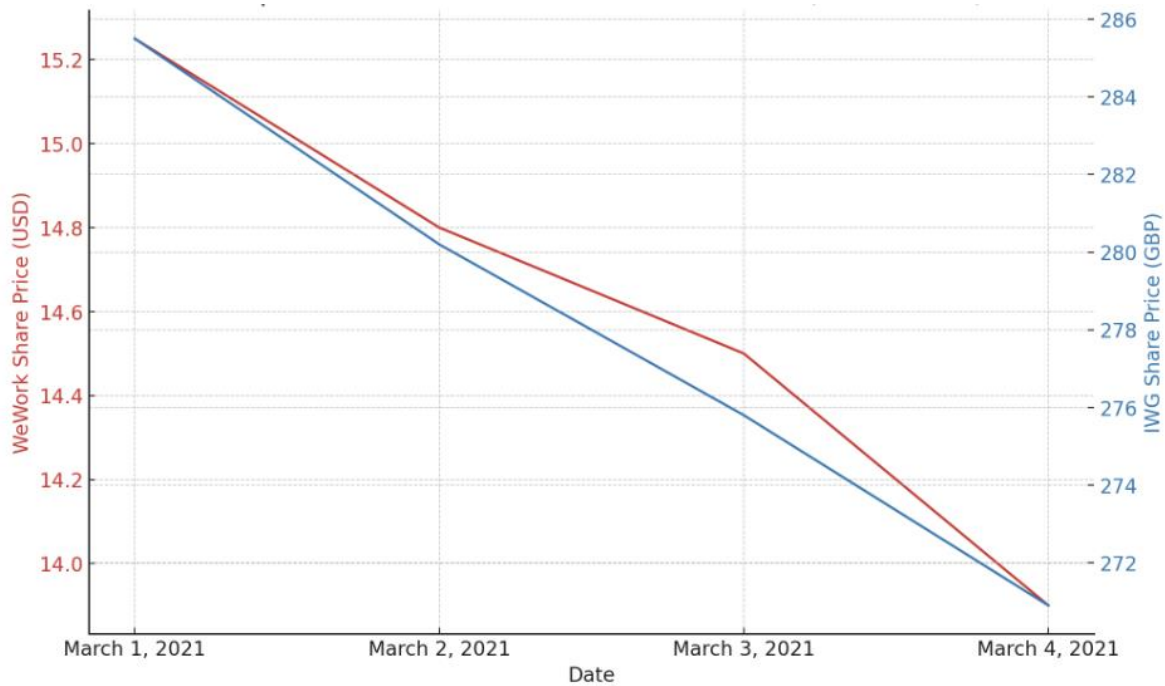
Figure 3. Quarterly Rev. and Net Income before bankruptcy



### **SPILOVER EFFECTS: HOW WeWork's FINANCIAL DIFFICULTIES AFFECTED IWG'S SHARE PERFORMANCE ON THE LONDON STOCK EXCHANGE**

WeWork's financial troubles cast a shadow over the London Stock Exchange, particularly affecting the shares of IWG, a key player in the co-working space sector and a competitor. Despite its strong financial position and proactive management, IWG suffered from investor anxiety, driven by perceived similarities to WeWork's operating model and market segment. This 'guilt by association' led to a decline in the value of IWG's shares, as evidenced by the simultaneous decline in the share prices of both companies, even though IWG operates a distinctly different business model under the Regus brand. Mark Dixon, CEO of IWG, vigorously defended the company, emphasising its long-standing profitability and fundamentally sustainable business approach, different from that of WeWork. However, market scepticism, fuelled by WeWork's high-profile difficulties, underlines the challenge IWG faces in disassociating itself from the stigma affecting the industry, highlighting the complex dynamics at play in investor behaviour and market sentiment within the London Stock Exchange.

Figure 4. Comparison of WeWork and IWG share prices (March 2021)



## CONCLUSION

The rise and subsequent challenges of WeWork underscore vital lessons about the balance required in innovative enterprises, particularly in the co-working industry. While WeWork's rapid growth and novel approach initially disrupted the market, its struggles highlight the essential need for sustainable business models and effective management to support innovation. Thus, the WeWork case study reminds us that the success of any company, especially in dynamic sectors such as co-working, depends on its ability to innovate responsibly and adapt continuously, ensuring that its business model remains progressive and resilient in the face of market changes.

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