

Office leasing opportunities amid Covid surge

E-commerce, outsourcing and data centres to drive demand post-COVID

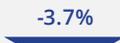
Insights & recommendations

Colliers saw the highest transaction level in the first quarter since the lockdown began last year. However, the surge in cases in Q1 2021 halted the gains. In our view, Metro Manila's office market demand recovery hinges on the pace of the Covid-19 vaccination program. Increasing vaccinations should reduce the number of Covid cases and bolster confidence for companies to return to the office.

Colliers encourages tenants to:

- Assess their revival and growth prospects to take advantage of tenant-favorable office market (e.g. blend-and-extend.)
- Consider short-term lease options (e.g. 1-to-2-year terms or flexible workspace) to tide over space needs in an uncertain period.
- Implement the hub-and-spoke strategy to tap new labor sources and reduce real estate costs.
- Employ flight-to-value and/or flight-to-quality strategies.



	Q1 2021	Full Year 2021	2021-25 Annual Average
 <p>Demand</p> <p>E-commerce, outsourcing and data centers drove demand in Q1 2021. However, net absorption remained negative because of lease cancellations and/or non-renewals. Colliers sees net take-up recovering by the end of 2021, especially with the successful roll out of the Covid vaccine.</p>	 <p>-52,800 sq metres</p>	 <p>351,300 Sq metres</p>	 <p>653,300 Sq metres</p>
 <p>Supply</p> <p>From 2021 to 2025, we project the annual completion of about 641,200 sq metres (6.9 million sq feet) of new office space. We project Fort Bonifacio, Quezon City and the Bay Area to account for about 47% of the new supply during the period.</p>	 <p>199,900 sq metres</p>	 <p>878,200 sq metres</p>	 <p>641,200 sq metres</p>
	QOQ / End Q1	YOY / End 2021	Annual Average Growth 2020-25 / End 2025
 <p>Rent</p> <p>Existing tenants continue to rationalize office space by not renewing unused spaces and exercising pre-termination option. Rents continued to decline in line with the Colliers projection of 15% reduction in 2021. Colliers expects rents to recover starting 2022.</p>	 <p>-3.7% PHP908</p>	 <p>-15.0% PHP797</p>	 <p>+0.5% PHP967</p>
 <p>Vacancy</p> <p>Colliers projects vacancy in 2021 reaching 12.5% due to lease non-renewals, cancellations, pre-terminations and substantial new supply coming online. We see demand coming from E-commerce, outsourcing, data centers and even POGOs moving forward which should temper vacancy increases in 2022.</p>	 <p>+2.9pp 11.0%</p>	 <p>+3.4pp 12.5%</p>	 <p>-0.5pp 6.8%</p>

Source: Colliers

Note: USD1 to PHP48 as of the end of Q1 2021. 1 square m = 10.76 square ft. *Also known as Philippine Offshore Gaming Operators (POGOs), primarily offshore gaming firms from China. Traditional (includes companies in various sectors such as legal, engineering and construction, government agencies and flexible workspace operators), POGO, and outsourcing firms.

Recommendations

Blend and extend

We recommend that tenants take this opportunity to use a blend and extend strategy; (e.g negotiating lower rents in exchange for longer-term commitments). Colliers believes that landlords should be more open to this concession requested by tenants amid a challenging leasing market. Landlords should consider this an opportunity to lock in key tenants including those from segments that continue to thrive amid the pandemic, such as e-commerce and logistics.

Tenants to take advantage of opportunity to negotiate

Given the 878,200 sq metres (9.4 million sq feet) of new supply likely to be completed in 2021, Colliers encourages tenants to maximize favorable market trends by negotiating lower rates, longer lease terms and other forms of concessions such as delayed escalation of rents, rental deferral, fit-out financing longer fit-out periods and other incentives. Companies with long-term lease plans should also maximize the opportunity to transfer to higher quality buildings in major business districts at a discount.

Diversification in location

Companies have been minimizing the size of their central locations in major business hubs and are looking for other sites either Northern or Southern Metro Manila. Colliers believes that among the viable alternative locations in Metro Manila include Quezon City and Alabang. Landlords, meanwhile, should be proactive in identifying demand outside of Metro Manila. We encourage developers to further explore the viability of building offices in Bulacan, Pampanga, Laguna, and Iloilo to capture demand from firms locating outside Metro Manila.

Short-term options to assess post-pandemic operations

Colliers believes that firms taking a wait-and-see and assessing post-pandemic

options should consider short-term leases. In our view, this approach can tide them over during the most uncertain 1- to 2-year period. They may opt to renew short-term or sign up in flexible workspaces to minimize capital expenditures and save on operating expenses. Among the locations with a substantial amount of vacant serviced offices are Makati CBD and Ortigas CBD.

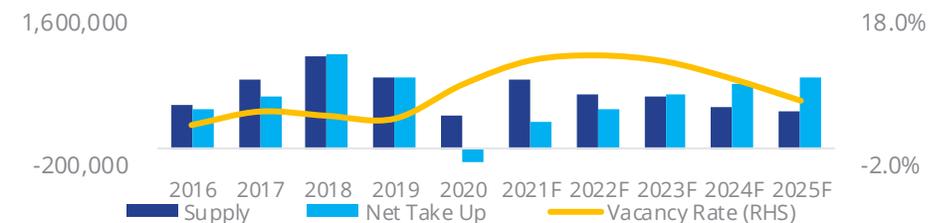
Developers spreading out office portfolio

In Q1 2021, Colliers saw the completion of about 199,900 sq metres (2.2 million sq feet) of new office space. Makati CBD and the Bay Area covered 75% of new supply during the period with the completion of Armstrong Corporate Center, AO2 The Central, Ayala Triangle Gardens 2 and Centrium North and South Towers. Colliers also recorded the completion of Blakes Tower and The Stiles Enterprise West Tower in Makati Fringe and the GSC Corporate Tower in Fort Bonifacio.

In 2021, we project new supply to reach 878,200 sq metres (9.4 million sq feet), down from our initial estimate of about 886,200 sq metres (9.5 million sq feet) at the end of 2020. In our opinion, buildings with low pre-commitment levels and those in the early stages of construction are likely to compel landlords to defer completion timelines until market conditions improve.

From 2021 to 2025, we see the delivery of 641,200 sq metres (6.9 million sq feet) of new office space per annum, down 3% from our previous forecast of 658,300 sq metres (7.1 million sq feet) in Q4 2020. The Bay Area, Fort Bonifacio and Quezon City will likely account for close to 50% of the new supply during the period.

Metro Manila office forecast (square metres)



Source: Colliers

E-commerce, data centres to drive demand

In Q1 2021, lease transactions in Metro Manila reached the highest mark during the pandemic but net take-up remained negative for the fourth consecutive quarter due to higher lease cancellations, non-renewals and pre-terminations. In Q1 2021, net take-up reached -52,800 sq metres (-568,100 sq feet) as traditional, outsourcing firms and POGOs continue to vacate office spaces. This figure is also lower than the 125,200 sq metres (1.3 million sq feet) of net take-up recorded in Q1 2020.

Colliers has observed that e-commerce, outsourcing and data centres absorbed spaces in Q1 2021. In our view, firms from essential segments are likely to lead office take up in the next 12 months.

In Q1 2021, we saw e-commerce firms such as Shopee and Amazon leading office space take-up while substantial space take-up was observed from traditional occupiers, data centres and even POGOs. Most of these firms occupied spaces in Ortigas CBD, Fort Bonifacio and Quezon City. Traditional firms covered about 68,400 sq metres (736,00 sq feet) of office deals or 44% of total transactions in Q1 2021.

In our opinion, data centres are also likely to drive office space demand moving forward as they expand in developing countries such as the Philippines to cater to the growing demand. In Q1 2021, we have recorded about 19,000 sq metres (204,400 sq feet) of office deals from data centres in Ortigas Fringe.

While some outsourcing firms continued expanding, some of them continue rationalizing office spaces as they carry out work-from-home (WFH) strategies and comply with government-mandated health protocols. Colliers believes that outsourcing firms are likely to continue these measures until all employees have been vaccinated against Covid.

Colliers has noted that outsourcing firms have been occupying office spaces outside Metro Manila due to less disruption in business operations caused by the rising Covid cases compared to Metro Manila.

Among the firms that took up office space are Legato and Teledirect in Iloilo, 24/7 InTouch in Cebu, Sitel Philippines in Tarlac and TaskUs in Batangas.

The increasing number of pre-terminations and the substantial new office supply that came online across Metro Manila totaling 199,900 sq metres (2.2 million sq feet) has resulted in a vacancy of 11.0% in Q1 2021 from only 9.1% in Q4 2020. Colliers believes that office vacancy will likely increase to 12.5% at the end of 2021 due to the projected new supply of 878,200 sq metres (9.4 million sq feet) and our estimated net take-up of about 351,300 sq metres (3.8 million sq feet). Colliers also sees the Bay Area and Ortigas CBD likely recording higher vacancies due to the significant new supply over the next 12 months.

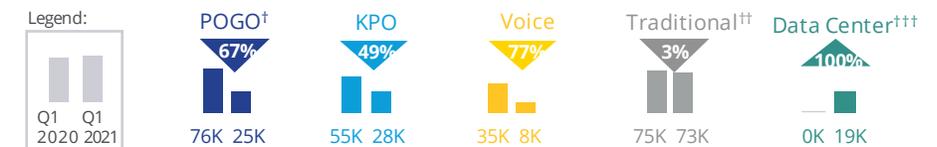
Rental recovery delayed to 2022

Office rents on average have declined by 3.7% QOQ in Q1 2021. We project a further correction in lease rates especially in submarkets with high vacancies due to lease cancellations (e.g. Quezon City, Fort Bonifacio and Makati Fringe) and significant amount of upcoming supply (e.g. Bay Area and Ortigas CBD). In 2021, we see office rents dropping by 15% before a slow recovery in 2022.

Colliers has observed that some landlords have been offering more favorable commercial structures to tenants such as lower base rents, delayed escalation, longer fit-out and rent-free periods, fit-out financing, and other customized incentives just to attract more tenants.

Colliers believes that office leasing recovery beyond 2021 will likely hinge on the pace of the Covid inoculation, especially the inclusion BPO employees² in the vaccination priority list and developments in the recently enacted CREATE law.

Metro Manila office transactions



Source: Colliers; [†]Also known as Philippine Offshore Gaming Operators. ^{††}Traditional occupiers includes companies such as legal, engineering and construction, government agencies and flexible workspace. ^{†††}Data Centers are facilities that house computer, telecommunications and storage systems.

¹CREATE = Corporate Recovery and Tax Incentives for Enterprises

²[BPO sector pushes for inclusion in vaccination priority list](#)



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