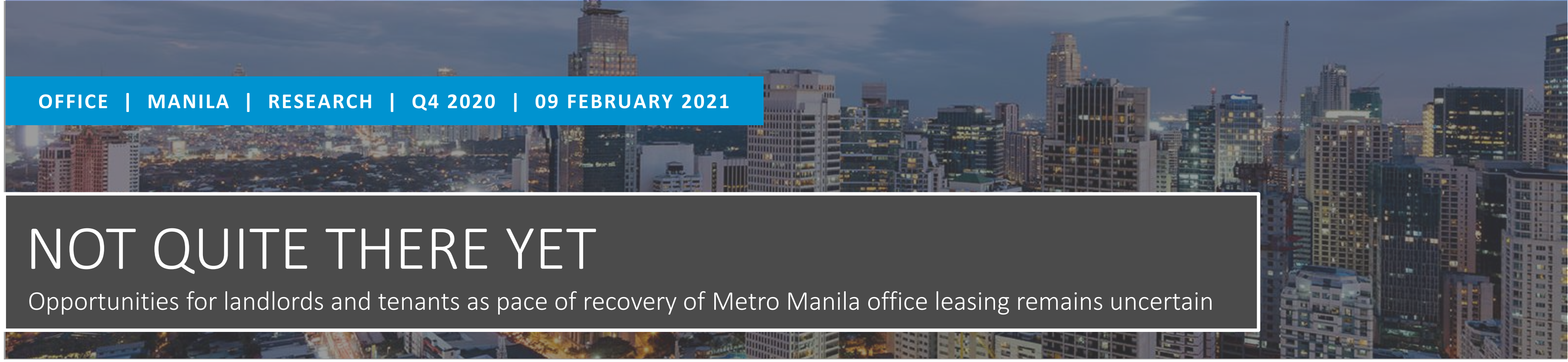


OFFICE | MANILA | RESEARCH | Q4 2020 | 09 FEBRUARY 2021

NOT QUITE THERE YET

Opportunities for landlords and tenants as pace of recovery of Metro Manila office leasing remains uncertain

Joey Roi Bondoc
Associate Director | Research | Philippines
+63 2 8858 9057
Joey.Bondoc@colliers.com

Dom Fredrick Andaya
Director | Office Services | Philippines
+63 917 831 6725
Dom.Andaya@colliers.com

Insights & Recommendations

We continue to see an uncertain office leasing environment in Metro Manila over the next 12 months. Despite this, we see some firms, especially those that provide essential goods and services, expanding and absorbing office space.

Overall, the decrease in demand will likely result in a rental correction in 2021 before our predicted recovery which should start in 2022.

Amid a challenging market, we recommend landlords and tenants focus on opportunities in the current market environment.

Landlords should be proactive in offering alternative leasing models to tenants; be flexible to tenants' request for concessions; and adjust construction pipelines to prevent further erosion of rents across the capital region.

		Q4 2020	Full Year 2021	2021-25 Annual Average
Demand	> Firms providing essential goods and services are likely to drive office space absorption in 2021. We see cost-sensitive firms occupying vacated but fully-fitted spaces in key business districts such as Fort Bonifacio.	-70,700 sq meters	354,500 sq meters	732,300 sq meters
Supply	> Colliers sees the delivery of about 886,200 sq metres (9.5 million sq ft) of new office supply in 2021. We estimate that about 67% of the new supply will likely be in the Bay Area, Fort Bonifacio, and Ortigas CBD.	189,200 sq meters	886,200 sq meters	658,300 sq meters

		QOQ/ End Q4	YOY/ End 2021	Annual Average Growth 2020–25 End 2025
Rent	> Subdued leasing across all segments (traditional, POGO, and outsourcing)* is likely to result in a correction of lease rates. We project rents to bottom out in 2021 before a recovery starting 2022.	-6.2% PHP851	-15.0% PHP724	+0.8% PHP886
Vacancy	> Colliers projects vacancy in 2021 to rise as POGOs continue to vacate office space and outsourcing firms rationalize office requirements. We expect vacancy to reach 12.5% in 2021, the highest since 2003.	+2.0pp 9.1%	+3.4pp 12.5%	-0.6pp 6.2%

Source: Colliers International. Note: USD1 to PHP48 as of the end of Q4 2020. 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

Alternative leasing schemes and expansion sites

Colliers has observed that while most leasing is momentarily paused, some occupiers are still actively looking for office space, especially those from the essential industries and companies that plan to implement alternative schemes such as a hub and spoke model. Colliers encourages landlords to expand tenants' options by offering available office space in non-core locations where rates are 30% to 50% cheaper than major business districts. This is important especially for companies planning to implement a hub and spoke leasing scheme wherein occupiers reduce the reliance on a single headquarters for a more dispersed occupancy strategy.

Be more flexible to tenants' request for concessions

In our view, tenants continue to take a wait and see stance and look for opportunities to reduce costs while aligning their leasing strategies with their business plans. We see tenants exploring short term (e.g. six month) lease renewals during this period of uncertainty, complementing traditional offices with remote work models. Meanwhile, the companies that are still expanding are likely to renew leases and take advantage of opportunities to negotiate a more reasonable commercial structure that is attuned to market conditions such as a lower base rent, delayed escalation, fit-out financing and rent-free incentives. In our view, landlords should be more proactive in accommodating tenants' requests for concessions to prioritize healthy levels of occupancy during this period.

Landlords to be mindful of new supply

From the bitter experience during the Asian Financial Crisis (AFC), developers quickly understood the need to turn off the supply tap. This was evident in 2010 after the Global Financial Crisis (GFC) when office completion dropped to 203,000 sq metres (2.2 million sq feet) from 523,000 sq metres (5.6 million sq feet) in 2009 as projects were deferred or outright cancelled. Colliers encourages landlords to be mindful of their office supply pipeline, balancing new development with their building's pre-leasing status and the overall pace of leasing recovery.

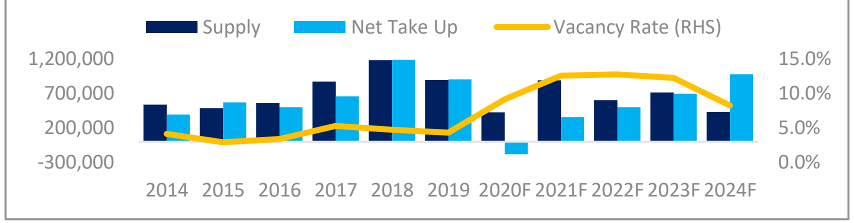
Maximize proximity to infrastructure projects

Colliers encourages developers to maximize the proximity of their buildings to upcoming key infrastructure projects due to be completed in Metro Manila. From 2021 to 2022, Colliers sees the completion of the LRT-2 East Extension, NLEX-SLEX Connector Road, Skyway SLEX Extension, Estrella-Pantaleon Bridge, and the BGC-Ortigas Link Bridge. Among the locations that are likely to benefit from the completion of these projects are Fort Bonifacio, Alabang, Ortigas CBD, and Quezon City. Developments in these areas should allow landlords to highlight the advantages of their proximity to public infrastructure and lure the workforce back to traditional offices.

Tap essential segments' office requirements

In 2020, Colliers recorded 27,000 sq metres (290,500 sq feet) of office space deals from traditional occupiers providing essential services such as healthcare, e-commerce, financial technology (fintech), telecommunications and logistics & warehousing. We project demand from these sub-segments to be sustained over the next 12 to 24 months as these are likely to be driven by a lockdown and household consumption-led economy. Hence, developers should proactively target these companies' office space requirements moving forward.

Metro Manila office forecast (square metres)



Source: Colliers International

PARED DOWN SUPPLY

In Q4 2020, Colliers recorded the completion of about 189,200 sq metres (2.0 million sq feet) of new office supply. The Bay Area contributed 33% to new supply during the period with the completion of Uzume Building, Aspire Corporate Plaza and Platinum Tower. Colliers also saw the completion of BGC Corporate Center 2, One Le Grand Tower in Fort Bonifacio, Kingston Excell Building in Alabang, Cyber Omega in Ortigas CBD, and Baja Corporate Center in Makati Fringe. In 2020, new supply only reached 425,500 sq metres (4.6 million sq feet), down 60% from our initial estimate of 1.07 million sq metres (11.5 million sq feet) at the start of 2020 as the pandemic hampered the completion of new buildings.

In 2021, we project the completion of about 886,200 sq metres (9.5 million sq feet) of new supply, down 16% from our initial forecast of about 1.05 million sq metres (11.3 million sq feet) at the start of 2020. Colliers believes that some landlords are inclined to complete buildings that are already on the final stages of construction or have achieved a decent level of pre-commitment as of the end of 2020.

From 2021 to 2025, we see the delivery of about 658,300 sq metres (7.1 million sq feet) of new office space annually, down 13% from our initial estimate of 757,500 sq metres (8.2 million sq feet) at the start of 2020.

VACANCY TO RISE IN 2021

Office space absorption continued to slide for the third consecutive quarter in Q4 2020 with net take-up turning negative. For 2020, we recorded a net take-up of −183,100 sq metres (−1.9 million sq feet), down 120% from the 899,600 sq metres (9.7 million sq feet) absorbed in 2019. 2020 was also the first time that we recorded a negative take-up on an annual basis.

Colliers saw traditional companies leading office space take-up in Q4 2020 especially firms under the e-commerce, healthcare, telecommunications, fintech, and logistics industries. Most of these firms occupied spaces in Makati CBD, Ortigas CBD, and Fort Bonifacio.

Meanwhile, no POGO transactions were recorded for the third consecutive quarter. In our opinion, the Supreme Court (SC) ruling imposing a temporary restraining order (TRO)[1] on the 5% franchise tax on gross gaming revenues from POGOs will likely prompt these firms to reconsider leaving the Philippines, but the bigger issue remains the lack of Chinese manpower due to travel restrictions.

Vacated spaces continue to outpace absorbed spaces in Q4 2020. The bulk of the office spaces vacated during the period were in Makati CBD, Alabang, and Quezon City. Meanwhile, we recorded a total of 314,000 sq metres (3.4 million sq feet) of office space vacated by POGOs at the end of 2020 from only 154,000 sq metres (1.7 million sq feet) at the end Q3 2020.

Colliers believes that among the business districts that are likely to lead recovery in 2021 are Makati CBD, Fort Bonifacio, and Ortigas CBD. A mix of traditional and outsourcing firms have pre-leased office space in these business districts. We see this trend continuing over the next 12 months.

[1] *Supreme Court stops higher POGO taxes*

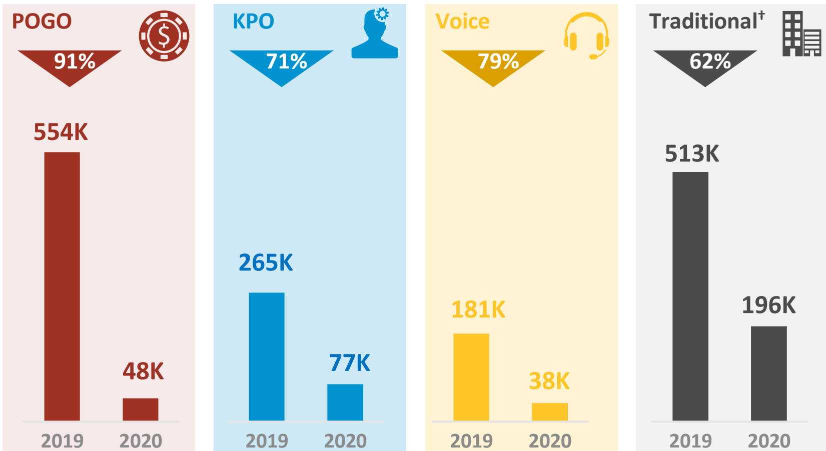
The substantial office space coming online across Metro Manila of about 886,200 sq metres (9.5 million sq feet) and our projected net take-up of 354,500 sq metres (3.8 million sq feet) should result in a vacancy of 12.5% in 2021, up from 9.1% in 2020. Our projected vacancy in 2021 is likely to be the highest since the 13.8% recorded in 2003.

RENTS TO BOTTOM OUT IN 2021

Office rents on average dropped by 17% in 2020. We expect a further correction in lease rates especially in submarkets with high vacancy due to lease terminations (e.g. Quezon City, Makati Fringe and Alabang) where a substantial amount of office space was vacated by POGOs and high levels of upcoming supply (e.g. Bay Area, Fort Bonifacio and Ortigas CBD).

Colliers has observed that landlords have become more flexible in accommodating tenants' requests to lower lease rates. These adjustments may come in the form of longer rent-free periods, fit-out allowances, delayed or waived escalation of rents, and other customized incentives to secure substantial occupancy of their buildings despite the delivery of significant new supply in 2021. We project a recovery in rents starting in 2022. The pace of recovery will likely hinge on the progress of rollout of a COVID-19 vaccine.

Metro Manila office transactions:



Source: Colliers International

† Traditional (includes companies in various sectors such as legal, engineering and construction, government agencies and flexible workspace operators), POGO, and outsourcing firms

Primary Authors:

Joey Roi Bondoc
Associate Director | Research | Philippines
+63 2 8858 9057
Joey.Bondoc@colliers.com

Dom Fredrick Andaya
Director | Office Services | Philippines
+63 917 831 6725
Dom.Andaya@colliers.com

Contributors:

Donica Cuenca
Research Analyst | Research | Philippines
+63 2 8858 9068
Donica.Cuenca@colliers.com

Martin Aguila
Research Analyst | Research | Philippines
+63 2 8863 4116
Martin.Aguila@colliers.com

For further information, please contact:

Richard Raymundo
Managing Director | Philippines
+63 2 8858 9028
Richard.Raymundo@colliers.com

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