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LOGISTICS LIFTS INDUSTRY

Logistics offsets manufacturing decline

Summary & Recommendations

The decline in foreign manufacturing commitments in the first three quarters of 2018 was offset by the rise in warehousing and logistics investment.

But as we see aggressive warehouse construction, Colliers believes that developers need to recalibrate their facilities to stand out and accommodate the demands of a fast-evolving e-commerce market.

Colliers encourages developers to continue constructing and upgrading warehouses; to scout for suitable land in Northern and Central Luzon and tie up with local developers; to push for the resolution of fiscal incentive issues; and to align expansion plans with the government's infrastructure push.

		Q4 2018	Full Year 2019	2018–21 Annual Average
Demand	> Colliers sees the bulk of foreign manufacturing pledges, particularly electronics and semiconductor investments, occupying industrial space in the region from 2019 to 2021.	4.04 ha	9.9 ha	9.5 ha
Supply	> We see limited increase in stock in CALABA (Cavite, Laguna, Batangas) from 2019 to 2021 due to the dearth of developable land. Much of the new industrial space is likely to be developed in Northern Luzon.	n/a	50 ha	50 ha

		HOH / End H2	YOY / End 2019	Annual Average Growth 2018–21 / End 2021
Rent	> Stable industrial supply coupled with rising demand should propel industrial land leasehold and factory rates at 3.5% per annum from 2019-2021.	4.0% PHP78	3.5% PHP81	3.5% PHP86
Vacancy	> We see overall vacancy in CALABA to decline further from 2019 to 2021 as manufacturing investments committed in 2017 and 2018 start to absorb industrial space.	-0.6pp 6.0%	-0.5pp 5.5%	-0.25pp 5.0%

Source: Colliers International
Note: USD1 to PHP53 as of end-Q4. 1 sq m = 10.76 sq ft; pp = percentage point.

RECOMMENDATIONS

Align expansion plans with the government's infrastructure push

Colliers believes that industrial developers and locators (a.k.a. manufacturers) should align their expansion plans based on the government's infrastructure push. A number of key projects due to be completed over the next two to three years will likely be in the Clark and Subic corridor, including Clark Airport Modernization, NLEX-SLEX Connector Road, and Subic-Clark cargo rail. Hence, it would be prudent for developers and occupants to explore available land and warehouses in the Northern Luzon corridor.

Explore potential partners and developable land in Northern Luzon

Due to the dearth of available industrial land in Southern Luzon, industrial park developers should explore parcels of land in the Northern Luzon provinces of Bataan, Pampanga, Tarlac, and Pangasinan that could be developed into industrial parks. National players should also consider partnering with the local developers and landowners. National players should leverage their vast experience in developing and managing industrial spaces in Southern Luzon that accommodate high-value manufacturers including electronics and semiconductor firms.

Developers to build more modern warehouses

We recommend that developers expand their footprint in the industrial segment by building more warehouses. Colliers projects demand for industrial warehouses to expand over the next 12-36 months due to the country's thriving e-commerce market. In H2 2018, Double Dragon completed its first warehouse in Tarlac and will likely open eight more facilities through 2020. Meanwhile, Robinsons Land will probably open two facilities in Calamba, Laguna. As developers construct more warehouses, Colliers encourages them to ensure that the facilities meet the demands of modern logistics and e-commerce.

MANUFACTURING DOWN, LOGISTICS UP

In the January to September 2018 period, data from the Philippine Statistics Authority (PSA) show that foreign investment commitments into the Philippines rose 8.2% to PHP91 billion (USD1.72 billion) from PHP84 billion (USD1.58 billion) in the same period in 2017. Manufacturing pledges during the period dropped to 37% to PHP29.6 billion (USD558.49 million) from PHP46.7 billion (USD881.12 million) in the same period in 2017.

The Philippine Economic Zone Authority (PEZA), one of the country's investment promotion offices, has attributed the decline to the uncertainties surrounding the enactment of the second package of the government's tax reform programme which aims to rationalize fiscal and non-fiscal incentives granted to economic zone locators. According to a survey by the Japan External Trade Organization (JETRO), fewer Japanese firms in the Philippines plan to expand over the next 24 months due to labor and tax reform issues. According to JETRO, only 52% plan to expand operations in the Philippines from 2019 to 2021, smaller than the 63% who said the same for 2018 to 2019. Some 54% of respondents were manufacturers. According to the JETRO survey, 40% Japanese firms in the Philippines enjoy the existing tax regime, higher than Japanese firms expressing the same sentiment in Malaysia (13.8%), Thailand (12.5%), Vietnam (9.5%), and Indonesia (3.8%).

But the decline in foreign manufacturing pledges was offset by the increase in transportation and storage investments. Commitments into the sector expanded by 70% during January to September of 2018 to PHP2.2 billion (USD41.5 million) from PHP1.3 billion (USD24.5 million) in the same period of 2017.

According to the central bank, around 1% of retail transactions in the Philippines use electronic platforms. This should improve over the next two to three years due to robust domestic spending and improving internet and infrastructure spending through the country. These should propel the demand for more modern warehouses and an efficient transportation system. Hence, we see more investments into the transportation and storage segment from 2019 to 2021.

CALABA VACANCY AT 6%

Colliers is still receiving queries for acquisition of industrial land in Cavite and Laguna but the lack of supply in both provinces is compelling manufacturers to explore available industrial land in Batangas.

Batangas' industrial vacancy dropped to 7.0% in H2 2018 from 8.0% in H1 2018 due to continued flow of manufacturing investments. Over the past 12 months, a mix of Japanese and Chinese firms have committed to expand operations or open new facilities in the province. These include Murata and Ibiden Philippines that produce electronic components and Taiwan-based Kinpo group which manufactures laser printers and disk drivers. These investments are complemented by warehousing and logistics investments.

Comparative vacancy

Region IV-A	H2 2017	H1 2018	H2 2018
Cavite	7.3%	6.6%	6.0%
Laguna	5.0%	4.9%	4.5%
Batangas	10.1%	8.0%	7.0%
AVERAGE	7.9%	6.6%	6.0%

Source: Colliers International

Laguna remains the most preferred industrial location in Southern Luzon, but investment plans are being stalled by the lack of industrial land in the province. As of H2 2018, Laguna clocked in vacancy of 4.5% from 4.9% in H1 2018. Over the last 12 months, much of the industrial projects in the province involve the development of manufacturing and storage facilities on stand-alone industrial land or acquisition of properties previously owned by food and beverage companies. These include San Miguel Pure Foods building, which is a 20,000 sq meters (215,000 sq feet) manufacturing plant in Santa Rosa, Laguna. Other high-value locators expanding operations include manufacturers of motorcycle parts, semi-conductors, and LED gadgets. Colliers has also observed an increased inflow of manufacturing and logistics support investments in Laguna. These are investments from a mix of Japanese, Chinese, and French investors.

Cavite's industrial vacancy dropped to 6% from 6.6% in H1 2018. According to PEZA, manufacturers of electronics, fabricated metal, and aluminum products have committed to expand operations in Cavite and these firms should absorb additional industrial space over the next 12 to 36 months.

At the end of 2018, the Cavite, Laguna, Batangas (CALABA) corridor posted an industrial vacancy rate of 6%, down from 6.6% in H1 2018.

We still see Batangas posting the highest take-up of industrial land and warehouses based on investment pledges recorded with PEZA. Colliers projects overall vacancy in CALABA to hover around 5.5% over the next 12 months. We see vacancy declining further, to around 5%, from 2020 to 2021. Some electronics and semi-conductor firms' expansion plans should further improve industrial space vacancy in the region from 2019 to 2021.

MARGINAL INCREASE IN STOCK

We project a marginal increase in CALABA's industrial stock from 2019 to 2021. We expect only about 148 hectares to be added to the region's stock over the next three years, or close to 50 hectares per annum. We see Batangas cornering almost 60% of the new supply, followed by Cavite (27%) and Laguna (18%). Some of the new supply will likely come from the expansion of existing industrial parks in Cavite and Laguna. However, an opportunity for developers of industrial parks is to tie up with local governments for the acquisition and eventual development of industrial land subject to the local government's land use plans and ordinances.

Industrial lease rates (PHP per sq m)

Region IV-A	H2 2017	H1 2018	H2 2018	Growth (HOH)
Leasehold (Land)	72	75	78	4%
Lease Rates (SFB**)	244	254	263	3.5%

Source: Colliers International
** Standard Factory Building

LEASE RATES CONTINUE TO RISE

Stable industrial land supply coupled with rising demand has resulted in increasing lease rates for industrial land in CALABA. Colliers recorded a 4% rise in industrial land leasehold rate to PHP 78 (USD1.47) per sq metre per month from PHP75 (USD1.42) per sq metre per month in H1 2018.

Lease rates for Standard Factory Buildings (SFBs) and warehouses grew 3.5% to PHP263 (USD4.96) per sq metre per month from PHP254 (USD4.79) per sq metre per month in H1 2018.

From 2019 to 2021, Colliers expects lease rates for both land leasehold and warehouse to increase about 3.5% per year.

FOREIGN INVESTMENT PLEDGES UP, BUT MANUFACTURING DOWN

Colliers believes that committed foreign investments from the various investment promotion agencies is a good barometer of investments expected to materialize over the next two to three years. Colliers believes that the slower flow of manufacturing pledges could have an impact on the actual amount of industrial space and facilities occupied over the next 12 to 36 months. Investment agencies such as PEZA attribute the lower amount of manufacturing projects to uncertainty surrounding the implementation of the second phase of Tax Reform for Acceleration and Inclusion (TRAIN 2).

Colliers believes that the expansion of industrial land supply in Northern and Central Luzon should partially be facilitated by the construction of North Luzon Expressway (NLEX) and South Luzon Expressway (SLEX) Connector Road. Due to be completed in 2021, the NLEX-SLEX Connector Road is likely to provide improved access to Manila Ports and Manila and Clark International Airports and connect the two major industrial hubs in the country, the Clark-Subic corridor and CALABA.

Overall, despite uncertainties brought about by the proposed rationalization of fiscal incentives, we believe that a number of factors should help sustain the inflow of manufacturing and logistics investments over the next two to three years, these include:

> development of major infrastructure projects in Northern, Central and Southern Luzon

> Philippines' trade deals with Asian and European countries

> further improvement of the Philippines' viability as an investment hub in the region

> streamlining of the business registration process (e.g. enactment of Ease of Doing Business Act)

> development of alternative industrial hubs in Northern and Central Luzon

> sustained growth of manufacturing sub-sectors on the back of strong domestic consumption and the construction sector (food, chemicals and electronics, among others)

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