Colliers Bi-Annual

ILOILO | OFFICE

1Q 2018

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Colliers INTERNATIONAL

Accelerating success.

Awaiting Infrastructure-driven growth

Dinbo Macaranas Senior Research Manager

The office sector growth in Iloilo has been limited by the available supply in the province. While interest from investors remains strong, the limited supply has prevented any major take-up from business process outsourcers (BPO) looking to expand. Vacancy stands at 11% but much of the available space is in older buildings that may require significant upgrading before use. Newer buildings, on the other hand, are significantly leased even before completion. As noted in our previous report, Colliers believes that the Iloilo office sector is ripe for growth considering its reliable labour pool and its supportive local government. However, there are no new projects in the pipeline that could spur new office activity. We note the rising number of flexible-workspace sites that is reflective of a growing entrepreneurial community. In terms of major movements, we expect more significant growth in the medium to long-term, fuelled by improvements in infrastructure as plans for land reclamation and the building of a skyrail are underway.

Forecast at a glance

Demand

Interest from BPOs is still strong but the limited supply has prevented any growth in demand. We expect higher demand within two to three years as developers launch new projects in expectation of infrastructure developments.

Supply

Colliers projects 74,500 sq m (801,900 sq ft) of office GLA to be completed in 2018–2019 with national developers completing their projects in Mandurriao. Upcoming supply however is almost fully leased as much space is reserved for the expansion plans of existing players.

Vacancy rate

We expect vacancy to increase by one to two percentage points in the next two years given the strong demand from BPOs and the limited upcoming supply.

Rent

Rents range between PHP250 to PHP500 per sq m (USD0.46 to USD0.93 per sq ft) across shopping malls in Iloilo. We project 2-3% growth in rents over the next two to three years as new, better-quality supply is completed.

Office Supply Forecast, GLA (sq m)

LOCATION	AS OF 2016	2017	2018	2019	TOTAL
City Proper	9,400	1,200	-	-	10,600
Jaro	400	-	-	-	400
La Paz	2,000	-	-	-	2,000
Mandurriao	52,600	24,600	47,000	5,300	129,500
Molo	4,300	-	-	-	4,300
Overall	68,700	25,800	47,000	5,300	146,800

Source: Colliers International Philippines Research

National developers to drive supply

Total office stock in Iloilo City has reached over 94,000 sq m (1.0 million sq ft) of office GLA, with approximately 27% or over 25,800 sq m (277,700 sq ft) completed in 2017. Majority of Iloilo's office stock is in Mandurriao, primarily due to projects by the national developers Ayala Land, Megaworld and SM Prime. Another national developer, Robinsons, has a few office spaces in its Robinsons Place mall in Iloilo City proper. Local developers meanwhile also have a few office space developments spread between Mandurriao and the city proper with the likes of Plazuela de Iloilo (1 and 2), Cornerstone Business Center, The Crown Building and JC Building, among others.

From 2018 onwards, Colliers expects about 74,500 sq m (801,900 sq ft) of office GLA will be completed, all by national developers looking to expand their developments in Mandurriao, where new office and retail developments are emerging. The biggest of these are SM Strata Tower 1 and 2 with at least 22,000 sq m (236,800 sq ft) of office GLA each. The first tower is due for completion in mid-2018, and the second tower in late 2019. Alongside, Ayala Land is also looking to complete two towers with Atria Park District BPO 1 and 2, while Megaworld is due to complete Two Techno Place Office 1 and 2. Besides these developments, only smaller formats for mixed retail and office space use may be seen across Iloilo City. Examples include The Galleria at Atria Park and The Grid Iloilo also in Mandurriao, each with approximately 3,000 sq m (3,200 sq ft) of office GLA.

Minimal change in vacancy reflects need for new office space

Overall office vacancy in Iloilo stands at 11%, driven by available space in older buildings. This reflects a slight increase in vacancy, primarily driven by the completion of Festive Walk Phase 1 in 4Q 2017 totalling 10,800 sq m (116,300 sq ft), which by itself is already significantly leased out. Much of the other available supply consists of older buildings and/or cannot accommodate larger space needs. Colliers expects the increase in vacancy to be temporary as interest from business process outsourcers (BPO) has remained high with investors looking to expand into Iloilo. According to the local government, foreign investors, including Australian, Canadian and British investors have explored the possibility of expanding in Iloilo. Unfortunately, the absence of sizable new supply in the province at present has prevented new entrants.

We expect vacancy to hover between 8% and 12% over the next two to three years, as the 47,000 sq m (505,900 sq ft) of upcoming supply in 2018 is likely to be taken up by existing players and prospective investors. Existing players such as Hinduja Global Solutions, WNS, and Startek continue to be the major players in Iloilo with plans to expand within their existing developments. An estimated 23,000 professionals are employed by BPOs in Iloilo and Iloilo remains a centre for learning in the Western Visayas, being home to reputable universities. Thus, the province continues to be an attractive location for expansion.

Meanwhile, rents range between PHP250 and PHP750 per sq m (USD0.46 to USD1.39 per sq ft). Older stand-alone buildings typically command lower rents, and are usually located nearer the city proper. The PHP750 per sq m (USD1.39 per sq ft) rate is an outlier as most of the newer offices are between PHP400 and PHP500 per sq m (USD0.74 to USD0.93 per sq ft). Colliers believes however, that rents will grow by 3% to 5% annually over the next two to three years as new, better-quality supply will tend to push rents up.

Office Vacancy Rate in Iloilo, 4Q 2017

LOCATION	VACANCY RATE
Iloilo City	11%

Source: Colliers International Philippines Research

Government support, infrastructure plans to keep demand up

As noted earlier, interest from investors remains high in Iloilo. Investors have constantly considered Iloilo as a potential location for investment given that it consistently ranks among the highly competitive cities and municipalities in the Philippines as ranked by the National Competitiveness Council. Furthermore, the local government has been aggressively promoting the province as an investment destination. Just recently in early 2018, the Iloilo City Trade and Investments Board (ICTIB) was created to strengthen relationships with investors and attract more business into the city.

Furthermore, there are plans to upgrade the access to various locations in Iloilo with two planned infrastructure projects. Two key initiatives are expected to have a significant impact on the real estate landscape of Iloilo City, namely the (1) a 365-hecatare land reclamation project, (2) a three-line skyrail project connecting key villages in the city. The reclamation project is targeted to start in two years and will be located along the Iloilo Strait, traversing Ortiz, City Proper, and Calumpang. This will be a joint development project by Marikudo Realty and Development Corp., Sunwest Group of Companies and Van Oord, envisioned to create a mixed-use commercial development of offices, retail spaces, and even residential projects. The skyrail on the other hand, is envisioned to connect Ungka to the City Hall, Jaro to the City Center, and Mohon to the City Proper. The project has currently finished the pre-feasibility stage.

Colliers believes these factors are key to keeping up the office space demand in Iloilo. At present, office space is primarily driven by BPO expansion plans, government entities closing in customer facing spaces in malls, as well as smaller firms and entrepreneurs locating in co-working spaces such as Dojo 8, Bonds, and Idealist. However, to ensure continuous availability of supply, as well as upgrades, infrastructure improvements should entice developers to continue building.

Build, build, build

For a provincial location such as Iloilo where the pre-leasing market is not as active such as in Manila, it appears that demand is largely a function of readily available supply. And given the limited space available in the market, growth has been limited. Colliers believes Iloilo is still ripe for growth given a supportive local government, on-going interest from investors, and a reliable labour pool. Furthermore, the infrastructure plans will strengthen interconnection across locations and improve accessibility. Thus, we recommend that both local and national developers continue to build new office buildings to widen the options for existing BPO players and prospective investors. We suggest that they should not only consider Mandurriao or the City proper as locations for new projects. Notably, Jaro, Savannah, and Molo may also become alternative locations for office buildings given the improved accessibility.

Office Rental Rates in Iloilo, 4Q 2017

LOCATION	RENTS
Iloilo City	PHP250 - PHP750

Source: Colliers International Philippines Research; USD1=PHP50

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Vertical shift

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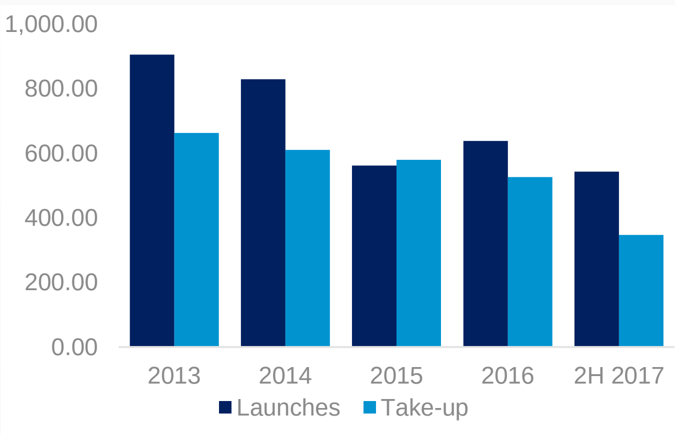
The Iloilo residential market is still largely composed of house and lots (horizontal). Interestingly, however, the provincial market has seen the rise of the condominium (vertical) market recently. While still in its early stages of development, the vertical market has notable bright spots. Fuelled by the growing business process outsourcing (BPO) sector and the huge community of OFW families in Iloilo, condominiums near the city centre have provided new options for Ilonggos. Especially for those living outside the city, the condominiums within the business district have become preferred alternatives. As demand is primarily supply-driven, Colliers recommends that developers continue to launch projects and ensure timely completion of vertical projects. Vertical developments projects near the business district should remain attractive, up to PHP6.0 million (USD120,000) or the mid-income segment. Meanwhile for horizontal developments, areas outside the city will continue to be preferred, particularly those under the affordable segment or PHP3.2 million (USD64,000) and below.

Iloilo Vertical Launches and Take-up, 2017 (units)



Source: Colliers International Philippines Research

Forecast at a glance

Demand

Demand is driven by the growing BPO workforce and OFW families. We expect increased demand upon completion of new condominiums in the Mandurrriao area. House and lots will continue to be viable in areas outside the business district.

Supply

Colliers projects over 1,900 condominium units to be completed by 2021 with national developers delivering their new projects in Mandurriao. This will expand the options to complement the over 20,000 units of horizontal developments already available in Iloilo.

Price

Total Contract Price (TCP) of condominiums currently stands at an average of PHP4.1 million (USD82,000). This shows a significant difference to house and lots which average PHP2.1 million (USD42,000). We expect this to increase by 5% to 10% annually in the next two to three years with condominiums within CBDs showing faster growth.

Iloilo Vertical Residential Supply Forecast (units)

LOCATION	AS OF 2017	2018	2019	2020	2021	TOTAL
Iloilo	1,890	290	950	290	430	3,850

Source: Colliers International Philippines Research

Emerging high-rise business district

The residential market in Iloilo is still primarily driven by house and lots which totalled 20,800 units as of end-2017. By contrast, condominium units have reached a mere 1,900 units. The proximity of condominium developments to Iloilo's business district has resulted in increased preference for condominiums among Ilonggos. This is driven by demand from BPO employees and OFW families who are looking to relocate into the city centre from municipalities outside the city.

However, we have noted an increase in the number of completions of condominium units in the last three years: completions averaged 425 units annually over that period,up from only 205 units between 2011 and 2013. The increasing number of condominium completions in the past years has helped stimulate demand. And with Iloilo continuing to be a primary source of the country's OFWs, particularly seafarers and nurses, coupled with the growing BPO workforce, today estimated at 23,000 employees – which has been growing together with the business district, it appears that interest for vertical development options will continue.

The pipeline in the next few years will continue to be robust. Upcoming condominium supply between 2018 and 2021 totals close to 2,000 units, reflecting a 100% increase from the current stock. Developments will be largely concentrated in the growing business district within Mandurriao. Some of the notable developments include Ayala Land's Avida Towers, Sta. Lucia's Soto Grande Iloilo, and Filinvest Land's One Spatial. Megaworld has the biggest share of the upcoming supply with over 1,000 units spread across their projects such as Lafayette Park Square, Saint Honore, and the first upscale development in Iloilo with an average price of above PHP6.0 million (USD120,000), The Palladium.

Supply-driven demand

Demand for Iloilo residential developments has been largely a function of supply. Take-up appears to be strong whenever projects are newly launched. In 2017, a total of three condominium projects were launched namely Megaworld's Saint Honore (South Wing) and Saint Dominique, and Filinvest Land's One Spatial (Building 1). For all these projects, take-up was strongest in the same quarter it was launched. For house and lot (horizontal) developments, on the other hand, only one project was launched in 2017, and take-up was also strongest in the second quarter, the same period when it was launched.

Overall, vertical developments have seen declining launches since 2013. Together with the decline in launches, take-up has slowed down. Between 2016 and 2017, launches of vertical developments saw a 15% decline to 543 units, while take-up saw a 34% decline to about 350 units year-on-year. It must be noted that both measures reached the lowest level since 2013 when launches reached 905 units and take-up reached 660 units.

Horizontal developments showed a very similar trend of decline. Launches declined by 58% to a mere 615 units in 2017 versus 2016. This level was from a high of close to 3,400 units in 2014. Take-up also was down by 26% in 2017 versus the prior year. Notably, take-up reached a high of 2,700 units in 2015. The drop in the number of launches and take-up among house and lot developments was partly attributable to the growing condominium market.

Iloilo Average Prices, 4Q 2017*

HOUSE & LOT	CONDOMINIUM	
(PHP / unit)	(PHP / unit)	(PHP/ Sq m)
2,300,000	4,100,000	112,100

Source: Colliers International Philippines Research;
*Actively selling residential units

Higher price segments to dominate upcoming condo supply

Upcoming supply until 2021 is primarily dominated by mid-income condominiums priced at above PHP3.2 million (USD64,000) to PHP6.0 million (USD120,000), reflecting a shift from prior years when delivered condominium units were limited to affordable and economic segments or those between PHP1.7 million (USD34,000) and PHP3.2 million (USD64,000).

Eight of nine projects due for completion between 2018 to 2021 are either mid-income or higher. This change in the residential options is reflective of a market where demand is shifting to the business district where prices tend to be more expensive.

Overall average total contract price (TCP) of actively selling condominiums stands at PHP4.1 million (USD82,000) as of 4Q2017. This is about 11% higher than PHP3.6 million (USD72,000) from 4Q2016. By contrast, the TCP of actively selling house and lots is merely PHP2.1 million (USD42,000). Colliers forecasts that there will be a 5% to 10% annual increase in prices in the next three years across various formats. We expect a faster increase in prices from vertical developments than from horizontal ones.

Affordable and mid-income sweet spot

As noted earlier, demand is primarily driven by the growing BPO labour force, with interest also coming from OFW families. While we note a shift in the market towards demand for condominiums, we still expect house and lots to be viable, especially in areas outside the city centre. The market is also slowly shifting to welcoming more expensive mid-income developments.

This is not surprising as Ilonggos' disposable incomes are also increasing. Data from the Philippine Deposit Insurance Corporation shows that the average bank deposits of individuals in Iloilo City has reached PHP121,000 (USD2,420) per account as of June 2017. This is up from PHP100,400 (USD2,008) three years ago in June 2014.

The breakdown of take-up in 2017 shows that for horizontal developments, the affordable segment is the most sellable with 45% of total take-up coming from those priced at between PHP1.7 million (USD34,000) and PHP3.2 million (USD64,000).

This is followed by 39% from the economic segment of between PHP450,000 (USD9,000) and PHP1.7 million (USD34,000).

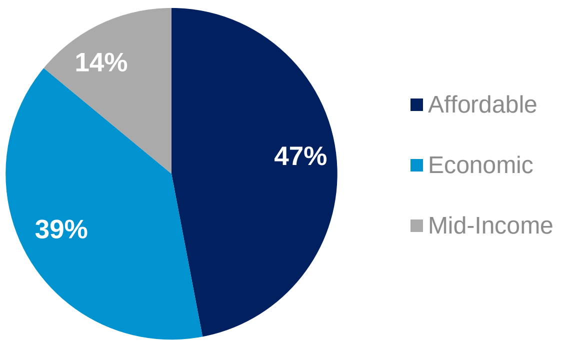
For vertical developments meanwhile, take-up in 2017 was led by the mid-income and affordable segments, extending the viable TCP price-point to as much as PHP6.0 million (USD120,000).

It is also interesting to note that despite the increasing price-point, most projects, whether horizontal or vertical, are performing very well with many already sold out and only a handful below 50% sold.

Location-driven strategy

In response to this shift in the market in terms of the type of development and the price-point, Colliers recommends that developers continue building vertical developments projects near the business district, where demand is strongest. For horizontal developments, areas outside the city will continue to be attractive, particularly those under the affordable segment.

Iloilo Horizontal Take-up per Segment, 4Q 2017



Source: Colliers International Philippines Research

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Local and tourist demand drives retail

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Iloilo's retail sector is dynamically changing with provincial brands competing healthily with bigger national and foreign brands. It is not surprising that well-established local developers with malls such as Mary Mart, Gaisano, and Amigo are also faring well alongside national players such as SM, Robinsons, Ayala, and Megaworld. Fuelled by rising income levels among Ilonggos, supported by the constant influx of tourists, it appears that the Iloilo retail scene will continue to thrive. In order to take advantage of these demand drivers, developers are ramping up their plans to build new malls both within and outside the city. About 79,800 sqm of retail GLA is expected to be completed within 2018. Colliers recommends that developers continue to allocate a portion of their space to local tenants alongside bigger foreign and national brands to cater to the diverse preferences of consumers. Meanwhile, we suggest that tenants carefully select their locations given the upcoming supply spanning San Rafeal, Pavia and Jaro. Furthermore, differentiation of retail offerings will be more important considering the upcoming supply.

Forecast at a glance

Demand

Increasing income levels of Ilonggos coupled with robust domestic tourism should drive retail spending in the province. Experiential retail formats such as exhibits, museums and theme parks should help differentiate retal offerings and drive demand.

Supply

Colliers projects over 79,800 sqm of retail space to be completed in Iloilo within 2018. Emerging locations include Jaro, Savannah and Pavia.

Vacancy rate

We expect vacancy to increase with the upcoming supply from 7% currently to 9% over the next two to three years.

Rent

RENT

Rents range between PHP350 and PHP850 per sqm across malls in Iloilo. We expect minimal growth of 1% to 2% over the next 12 to 36 months, considering the impact of new supply.

Iloilo Retail Supply (GLA, sq m)

	AS OF 2016	2017	2018F	2019F	TOTAL
Overall	217,000	22,500	78,900	-	318,400

Source: Colliers International Philippines Research

Mandurriao led-stock

Total retail stock in Iloilo City has reached close to 240,000 sqm (2.5 million sq ft) of GLA spanning all municipalities. The majority of this stock is in Mandurriao, primarily due to the 74,000 sqm SM City Iloilo. Other sizeable malls may also be found at the city proper with the likes of Marymart Center and Robinsons Place Iloilo, both with at least 20,000 sqm of retail space.

Collectively, retail spaces in Mandurriao total 132,000 sqm (1.42 million sq ft) or close to 56% of total retail stock. The section covering the west of Benigno Aquino Avenue, to the south of the Aleoasan road and north of the Iloilo River is of interest as it has a mix of outdoor and indoor mall offerings. Strip malls with a wide range of food and beverage options are popular locations for after work dinners, drinking sessions, and even family gatherings. Non-food establishments such as popular clothing brands and accessories are frequented in indoor malls.

In terms of upcoming supply, a total of 78,900 sqm (849,200 sq ft) of retail will be added within 2018 alone. Within Mandurriao, Megaworld's Festive Walk Mall will be the biggest with an estimated 28,000 sqm of retail mall space. Smaller formats are also being developed in the area with The Grid and The Galleria totalling an estimated 6,000 sqm (64,600 sq ft), both located in Brgy. San Rafael.

Other emerging locations are Pavia and Savannah. Double Dragon is building a City Mall and Robinsons is building another mall, both in Pavia. Vista Land is also constructing its own mall nearby with the Vista Mall Savannah. Colliers believes that these alternative locations outside the existing business districts will remain viable given the accessibility of these locations.

Vacancy expected to rise

Overall retail vacancy stands at 7% with the newer malls having pockets of available space. Bigger formats are close to full occupancy with most of them having less than 5% vacancy. The new neighbourhood malls which have merely partially opened typically have higher vacancy rates.

Interestingly, malls within the city proper are almost at full occupancy, filled with a bazaar-type set-up of ready-to-wear clothes, and gadget stores. Those outside the city proper have a mix of household foreign and local brands.

Looking ahead, we expect vacancy to rise, albeit marginally as new retail developments come in. The expected 78,900 sqm (849,200 sq ft) of retail space due this year should put upward pressure on vacancy rates. Considering the pipeline, we expect vacancy to move to 9% in the next two to three years. Neighbourhood malls, especially those in outdoor formats may have slightly higher vacancy than indoor malls as competition among food and beverage establishments has become tight, especially considering the wide range of restaurant options that are already available today. Colliers estimates that at least 25% of tenants in malls are food and beverage establishments.

Meanwhile, rents range between PHP350 and PHP800 per sqm (USD 0.65 to USD 1.49 per sq ft) Older malls typically command lower rents, while ground floor sites command the highest rents. Newer indoor malls command rents within the mid-range of the spectrum, averaging PHP500 per sqm (US0.92 per sq ft) level. It must be noted that rents at PHP800 (USD1.49 per sq ft) per sqm or above are outliers. Most malls have rents of between PHP400 and PHP600 per sqm (USD0.74 and USD1.11 per sq ft). Nonetheless, we see these outlier rents as indications of an attempt to push rents higher by charging a premium for good location and building structure. Colliers believes however, that rents will grow by a mere 1 to 2% in the next three years as growth will be tempered by the upcoming retail supply in Iloilo.

Local brands keep Iloilo's uniqueness

Iloilo City has tried to create a city centre similar to the centres of advanced cities such as Singapore's Esplanade, Sydney's Harbour Center and even Manila's Bay Area. It has its own version of the Baywalk and Esplanade with strips of outdoor retail establishments lining up the Iloilo river. Colliers believes that this strategy will continue to work especially considering the growing business activity in Iloilo, driven by the young professionals employed by business process outsourcers (BPO) and the strong domestic tourism.

Today, Iloilo has an estimated 23,000 BPO employees, a total which is still growing. Iloilo is also one of the most visited cities in Western Visayas. In 2017, tourist arrivals in Iloilo reached close to 640,000 with about 97% represented by domestic tourism. Furthermore, tourism receipts, or the value spend by tourists is estimated at PHP12 billion (USD 240 million) for the same year. Lastly, Iloilo is home to many OFW families, particularly seafarers and nurses. Hence, remittances should also continue to drive retail demand.

Given this background, it is not surprising to see the unique character of Iloilo's retail demand as it offers a mix of provincial local brands and foreign brands. As noted earlier, food and beverages is a growing segment in Ilolilo. National brands such as Mang Inasal, Jollibee, Goldilocks, J. Co. can co-exist with local favourites such as Kamalig, Madge Café, Ted's La Paz Batchoy, and Ramboys. It is also noteworthy that the co-existence of local and national brands is consistent across malls from different developers. Such a set-up may be found in Ayala's Shops at The Atria, SM Prime's SM City Iloilo and Southpoint, Robinson's Robinsons Place Iloilo, and Megaworld's Festive Walk. Tourists typically look for local restaurants to dine in while Ilonggo's may prefer national household favourites from time to time.

Meanwhile, regarding non-food retail establishments, fast fashion is emerging, especially in view of the entry of national developers in the retail scene. The likes of H&M and Uniqlo, which continue to be anchor tenants for the retail giant SM, have upgraded their clothing options in Iloilo. Colliers believes these foreign brands in newer malls can co-exist with the bazaar-type stores in the local malls such as Gaisano and Mary Mart as they target different customer profiles.

Differentiation in growing retail market

The outlook for retail also looks interesting as developers venture into theme parks and exhibits to continue to entice mall-goers. Megaworld is set to open Iloilo's first contemporary art museum as a key feature of the expansion of its Festive Walk strip mall. Robinsons on the other hand, is set to open a waterpark in its Robinsons Place Pavia which should differentiate its mall from others. These changes in the retail landscape should keep mall-goers interested. Moreover, especially for a clientele that consists partly of tourists, it will be good to add a few cultural elements to the retail tenancy mix.

Colliers recommends that developers continue to curate their tenancy mix to include local and national or foreign brands to cater to a diverse customer base. We also suggest that developers differentiate their malls by incorporating exhibits, and parks to enhance the experience of mall goers. The rich culture and history of Iloilo may also inspire features retail concepts. This should ensure that developers' malls continue to be patronised despite the sizeable upcoming retail supply which, in our view, will increase competition.

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