

*An Outlook towards the Office Market of
the Philippines' Queen City of the South*



Cebu Office Market: The Changing Landscape amid COVID-19

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Cover Photo by Zany Jadraque





Outside Luzon sits the Philippines' next biggest urban area, Metro Cebu. Home to almost a million square meters (sq. m.) of office space and thousands of companies, the metropolis, along with the region of Central Visayas, is among the highest contributors to the Philippine economy and is considered to be among the country's primary office markets. In 2018 alone it had contributed around 6.5% to the Philippine GDP, valued close to Php600 Billion. This was a growth of 7.6% year-on-year (y-o-y) of its own Gross Regional Domestic Product.

The office market in Cebu posted an occupancy rating of 90% for the 2H of 2019 and more than 260,000 sq. m. of upcoming office space for the rest of 2020. With two prominent business districts and more upcoming mixed-use township developments such as the Gateway Central, Mandani Bay, City di Mare and the growing Mactan Newtown, Cebu's office market is poised to expand even further.

Recognizing its economic importance, the

national government has initiated several key infrastructure projects in the area to further bolster its growth while providing another option, other than Manila, for investors and companies to invest and expand unto. The second Terminal building of the Mactan-Cebu International Airport as well as the recently renovated Terminal Building 1 are among those projects. Still, more are in the pipeline such as the Metro Cebu Expressway and the Cebu Bus Rapid Transit.

Metro Cebu was caught off-guard, however, when the COVID-19 pandemic struck and started to spread among the Philippine islands. Following the declaration of the State of Public Health Emergency and State of Calamity for the entire country as well as a number of presumptive positive cases within its borders, the city of Cebu has declared the State of Enhanced Community Quarantine (ECQ) in a bid to arrest the spread of the virus.

Cebu Under ECQ

Executive Order No. 64 Series of 2020 formally imposed the city of Cebu under an ECQ for a month starting from the 28th of March. A closure of businesses other than those deemed providing "essential goods" was also ordered prompting companies and large businesses to implement Work-From-Home (WFH) schemes. This in turn rendered office buildings empty except for a few skeletal personnel. In a matter of 2 days from the signing of EO 64, the streets of Cebu turned from having lanes of unending headlights to one devoid of life.

A significant drop in economic transactions soon followed and grappled the metropolis; and its aggregate damage still cannot be quantified. However, what is clear is that the longer the ECQ is imposed, the greater the damage figures will be. Companies are faced with financial pressure to continue operations for the continuity of their businesses. As the theory of evolution

overstates the “survival of the fittest”, so too is the implication of the business climate amid the COVID-19 crisis.

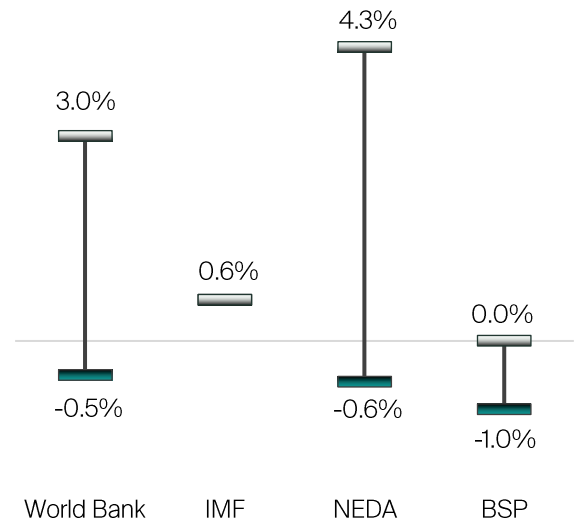
With some of their tenants finding it hard to continue operations and/or maintain their current office space take-up, landlords are faced with the possibility of increased vacancy. Unfortunately, with the anticipated drop in economic transactions for the rest of the year, the economic outlook for 2020 is dismal. The world institutions such as the International Monetary Fund (IMF) and the World Bank as well as the country’s National Economic Development Authority (NEDA) and the Bangko Sentral ng Pilipinas (BSP) all concur. This being said, the prospect of finding new tenants looks slim. Developers of upcoming developments, to be operational within the year, are seemingly troubled apparently from the expected low office occupancy levels of their projects.

Global Trend of Office Landlords showing Flexibility

As a way of avoiding vacancy surges, landlords have found it better to provide rent relief measures to their tenants as it would be easier for them to keep them rather than to go and look for a new one. Rent relief measures may come in the form of rent abatements, deferments and/ or discounts. At a time when companies are finding it hard to generate revenues as much as the previous years, rent relief measures help lessen the financial pressure of tenants, thereby prolonging their capacity to operate amid the ECQ.

With the rent relief measures in place, it is expected that headline office space lease rates in Cebu would freeze by the 1H 2020 with a possibility of contracting in the future months should the ECQ be continually imposed and/or market conditions continue to worsen. Gradually, these relief measures would also shift the market to one more favorable to tenants. As such, for some companies with excess amounts of

FIGURE 1
Forecasts for the 2020 Philippine GDP Growth/ Contract



Source: World Bank, IMF, NEDA, BSP

cash, this may be the time to do value-shopping and look for the best deals for office space in the market.

Improving Business Continuity Plans (BCPs) & the Use of Tech

The effects of COVID-19 crisis on the economies around the world has been one of the most economically damaging and it is not likely to be the last one. At a time when most of the world is interconnected and global markets are heavily reliant on one another, external shocks between economies are bound to happen. With the threat of the next crisis just lurking in the corner, improving business continuity plans should be a priority for companies to ensure safeguards are in place in times of uncertainty.

The use of technology to sustain operations have been practiced by most companies even before the implementation of ECQ. Most notable among them is the use of communication applications (apps) that allow instant messaging and video conferencing between employees and clients. With the imposition of ECQ still

ongoing, several companies have begun to use these apps as a means to reach the public and boost their online presence either through webinars or online press conferences. The use of these apps was also what made WFH schemes possible in the first place.

The Effects of COVID-19 Crisis Post ECQ

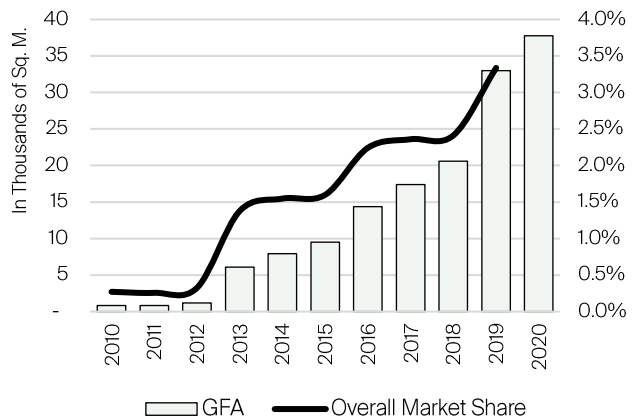
Securing facilities and property management services is expected to be a priority for landlords after the implementation of ECQ. Aside from the overall management and cleanup services, they provide a sense of security for the tenants that their offices are well maintained and they act as the “front liners” in keeping the threat of COVID-19 off from the building premises.

Developers may also pursue LEED, WELL and BERDE certifications for their existing and upcoming office spaces as future tenants may require certified office spaces for health and employee well-being purposes.

The implementation of ECQ has also caused delays in the upcoming office supply in Cebu. Originally at 260,000 sq. m., only 96,000 sq. m. of office space is seen viable to be operational within the year.

Even when the vaccine for COVID-19 is developed, physical distancing will continue to be practiced and become the new norm. As such, some companies may opt to continue implementing partial WFH scheme to limit the number of employees in their offices while others may find the WFH scheme to be effective in their business. Still, there may be other companies who will continue to fully implement WFH schemes and have their offices be filled only by a skeletal workforce. These arrangements may cause tenants to be more efficient in their office space utilization prompting them to lower their space requirements. As such, there is a

FIGURE 2
Co-Working, Flexible & Serviced Office Space’s Growth and their Overall Cebu Office Market Share



*2020 Figures cover only the months of January to March
Source: Santos Knight Frank Research

possibility that the Cebu office market may have temporary surges in vacancy levels.

Companies who found WFH schemes to be ineffective for their businesses, however, would need additional office spaces capable of providing all the necessary office equipment at the soonest possible time to comply with the physical distancing mandate. This is where flexible and serviced offices can take advantage of as these spaces come with private rooms and, with few modifications, provide enough space allocation for every employee. Additionally, cautious tenants, in a bid to mitigate risks in these times of uncertainty, could find shelter in flexible and/ or serviced offices.

Although Co-Working Office Spaces would suffer from low occupancy levels due to its emphasis on “collaboration”, which is not allowed under the physical distancing mandate, these spaces may still be converted to flexible and/ or serviced offices to generate more revenues. Other services, like the provision of virtual address for tenants, may be bolstered to secure more revenue streams.

Currently, there is an estimated gross floor area of around 38,000 sq. m. for Co-Working, Flexible and Serviced Offices in

Metro Cebu. This figure has continuously been increasing and in 2019 recorded a 60.27% y-o-y growth. However, with the COVID-19 virus looming, it is likely that this growth would contract as businesses try to survive and adapt to the new normal.

The Opportunities in Outsourcing Business

Similar as to what happened after the 2008 Global Financial Crisis, the Philippines may come out to be a top viable investment option for BPO companies. The pandemic has caused huge economic damages to other countries as well. Similarly, some major cities have also implemented their own versions of the ECQ to curb the spread of COVID-19. With such damages, these companies may look to cut costs by outsourcing some of their businesses here. As the metropolis already offers affordable office spaces and a high-quality of talent pool proven by the sizeable BPO workforce residing here, Cebu has already proven that it has the necessary manpower and infrastructure to cater to such businesses.

Coping with the Changing Landscape

Santos Knight Frank recommends to both the landlords and the tenants to open a line of communication to come up with a “win-win” situation for both parties in reviewing their lease agreements and terms. The symbiotic relationship between the two should be fostered and both should work closely to accommodate each other’s needs.

With a possible gradual increase in vacancy levels after the lifting of ECQ, landlords should actively seek out to retain their largest tenants as these companies would be crucial in keeping their properties financially afloat. As some companies may find WFH schemes effective in their business, landlords would have to be creative enough in either providing rent



relief measures and/or proposing the idea of flexible work spaces to keep tenants from moving out of their properties or lowering their space requirements.

BCPs are necessary for companies for them to navigate their businesses through the times of uncertainty. The experiences of companies from the past crises should be incorporated into consideration to improve BCPs. Utilizing technology to bolster company efficiency and employee productivity should also be continually enhanced.

The value of having facilities and property management services in office buildings can no longer be discounted. Their presence alone already radiates to tenants and other stakeholders that the property is well maintained. This should prove crucial now and in the coming months as companies would probably prefer well-kept office spaces for health and employee well-being reasons.

In these times of uncertainty, everyone is affected. Businesses, both tenants and landlords, will have to adapt to a new normal and do so quickly or face extinction. The COVID-19 pandemic has revealed to everyone just how vulnerable our industries are to external shocks. Nevertheless, this is not the first time the country has faced similar catastrophes nor will it be the last. The resiliency of the Philippine market will always prevail as it has done so in the past. We are all in this together and we will all get through it. 🇵🇭

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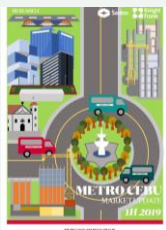
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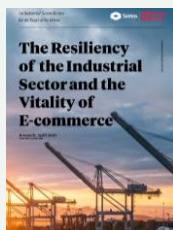
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