An Office Sector Review for the Pearl of the Orient

Metro Manila Office Sector Endures Despite Trying Times

Research, September 2020

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Metro Manila Office Sector Overview

The Metro Manila Office Sector was challenged to remain buoyant despite the threat of COVID-19. The implementation of Enhance Community Quarantine in March caused sluggish office take-up. However, through its well-built foundation and longevity, the office market was seen persisting during the 2Q of 2020.

Due to the strict government requirements concerning construction, no new office buildings were completed in the 2nd quarter. Despite the lack of new supply, however, the Metro Manila vacancy level continued its rise to 4.73% from 3.95% in the preceding quarter. Leasing transactions were mostly put on hold as companies took a wait-and-see approach towards new offices. The low levels of new office take-up led to a net loss of 50,047 sqm leased for the quarter.

There was also an increase in the number of sub-leases being offered in the market during Q2, as tenants looked to lessen their real estate costs by giving-up office space. These sub-lease opportunities, while not counted in official vacancy figures, do suggest a further softening of the office market during the quarter.

Notwithstanding the growing vacancies, office developers remained steadfast with respect to their asking rents. Thus, the weighted average lease rate in Metro Manila rose to Php 1,139 per sqm per month, translating to an increase of 0.79% quarter-on-quarter (q-on-q), and 5.75% year-on-year (y-o-y).

MAKATI

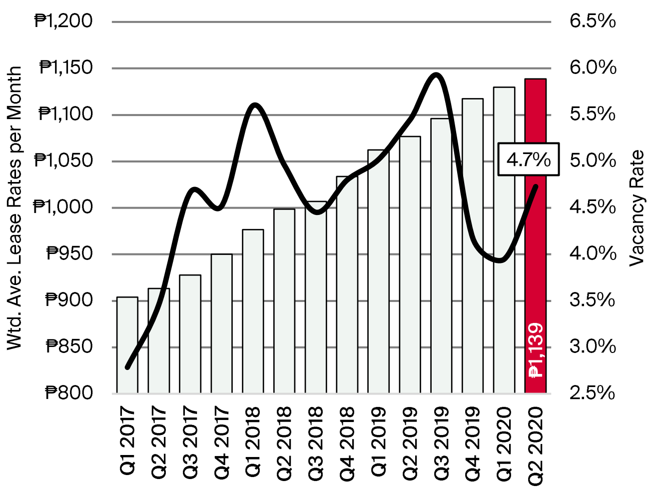
The most prominent business district in the country continued to command the highest headline rental rates in Metro Manila. Occupiers still held on to their prime properties during the quarter. Landlords in the CBD retained a same amount of Php 1,493 per sqm per month in the average monthly lease rate for 2Q 2020 with a 2.13% y-on-y growth. Additionally, the vacancy level further improved to 2.19% despite the threat of COVID-19.

The Makati CBD remains to be one of the most sought-after address by both multinational and local companies. Seeing this opportunity, developers are still keen in introducing more than 333,000 sqm of office supply in the next five years. Of this upcoming supply, around 89,000 sqm is anticipated to be operational by the end of the year.

FORT BONIFACIO

The impact of COVID-19 and subsequent lockdowns was slightly felt by the office sector in Fort Bonifacio. The aggregate

Figure 1
Metro Manila Office Lease Rate & Vacancy Level



Source: Santos Knight Frank Research

vacancy rating in the business district increased to 4.58% during 2Q from 3.97% in the previous quarter. But similar to the Makati CBD, weighted average rents still increased by 2.49% from the previous quarter to Php 1,274 per sqm per month.

In succeeding years, majority of office leases was seen to be driven by the upcoming office developments rather than existing ones. An estimated 540,000 sqm of office space is currently in the pipeline for Fort Bonifacio within the next five years.

BAY AREA

The demand and lease rate of the office sector in the Bay Area moved sideways from Q1 2020. Aside from the COVID-19 situation, international travel restrictions and resumption of POGO operations remained uncertain during the period. As of 2Q 2020, the average vacancy level in the business district was recorded at 0.59%. The average headline lease rate, on the other hand, was observed at Php 1,042 per sqm per month.

Despite the uncertainties, the Bay Area is foreseeing the highest upcoming new office supply in the metropolis. This is attributed to the availability of developable land in the area. Approximately 650,000 sqm of developments are expected to become operational for the next five years, 70,000 sqm of which are slated to come online this year.

ORTIGAS CENTER

Pre-terminations and non-renewals outweighed new leases during the 2nd quarter in the Ortigas Center. Vacancy levels rose to 5.10% , up from 2.97% of the preceding period. Ortigas thereby registered the highest increase in vacancies in the metropolis. Further, with no new buildings in the market during the quarter, there was a net loss of 22,569 sqm of leased space. Consequently, the average lease rate in Ortigas went down to Php 784 per sqm per month, the lowest among major CBDs in Metro Manila.

Around 623,000 sqm of upcoming office space is expected to come online in the Ortigas area over the next five years, including 100,000 sqm in 2020. This is the second highest supply pipeline after to the Bay Area.

QUEZON CITY

Similar to Ortigas Center, the office market of Quezon City experienced the same trend of rising vacancy levels and declining lease rates. Approximately 6,950 sqm of space was vacated during the quarter. This translates to an increased vacancy level to 9.98% from 9.35% from 1Q 2020. Additionally, the average lease rate declined to Php 949 per sqm per month, down by.09% q-o-q.

Approximately, 61,000 sqm of new office space is still expected to come online by the end of 2020 in Quezon City. This is part of the 395,000 sqm of upcoming space within the next five years, 47% of which will be coming from SM Prime Holdings.

ALABANG CBD

The office market in Alabang CBD exhibited the same trends as Fort Bonifacio. Rental rates increased despite the prolonged lockdown period. As of 2Q 2020, the average rent in the business district inched up to Php 859 per sqm per month. This translates to a 10.6% y-o-y rental growth, and 0.25% q-o-q increase.

This rental trend, however, has contributed to the increasing vacancies in the area. More than 9,000 square meters of office space were vacated during the quarter, pushing the aggregate vacancy level in the district to 5.42%.

Although Alabang has the potential to be a major CBD like Makati and Fort Bonifacio due to its vast available land remaining, it nonetheless has the lowest supply of upcoming offices. At present, slated projects in the next five years are estimated to boost office space supply by only 216,000 sqm, for which approximately 12,000 sqm is expected to complete in 2020.

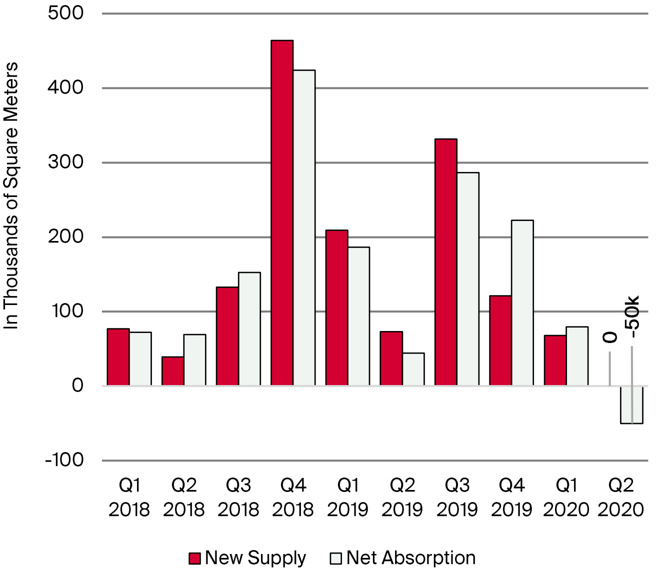
METRO MANILA OFFICE SECTOR OUTLOOK

Approximately, more than 472,000 sqm of Prime and Grade A Office spaces are expected to operate by the end of the year 2020, while 2.7 million sqm are anticipated to come online in the next five years. There may be no new office pipeline launches until at least the office market recovers and stabilize again.

The office rents in Metro Manila will is seen to be further exposed to demand pressures. Numerous landlords are still under-negotiation with their existing tenants. Although the forfeited cash deposits from pre-terminations may curb their loss of revenues in the initial months, the overall decrease in office demand for the rest of the year will still be felt by the lessors. Development and expansions will be set aside by most companies and improvement of business continuity plan will be prioritized. However, the shift to a tenant-favorable market is anticipated to uplift the medium- to long-term situation.

Figure 2

Metro Manila New Supply, Net Absorption & Vacancy Rate



Source: Santos Knight Frank Research

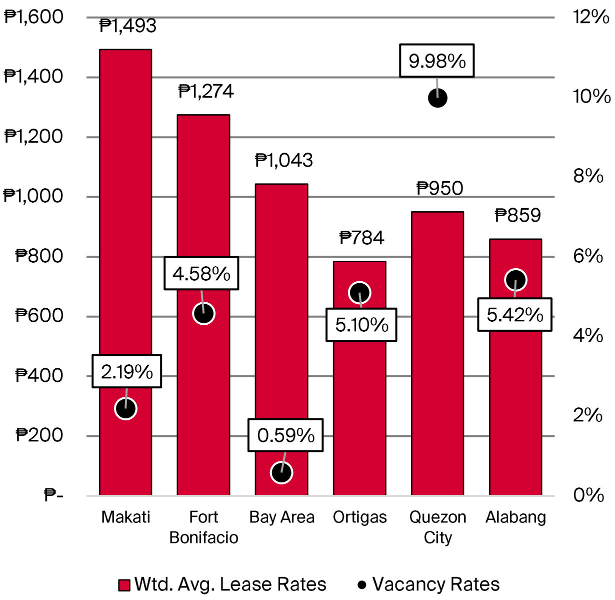
The POGO industry has portrayed an inconclusive role for the past months. Due to given high payable taxes by the Bureau of Internal Revenue (BIR), some operators have shut down their operations, resulting in more office vacancies for this quarter. POGOs may re-enter the country again or operate at a different entity but that will entail new license fees and additional capital expenditures on office spaces. The easing of international travel flights may bring back Chinese nationals to the country but the operations of the POGO will remain uncertain.

From a positive perspective, the IT-BPO industry is still foreseen as the major growth driver of the Philippine Economy and will continue to thrive as they adapt to the new normal. Amid these

unprecedented times, the majority of the outsourcing companies around the globe recognized the Philippines as a top location for office building developments. Developers should consider this opportunity to enhance and innovate their office spaces that will fit the new normal scheme and will attract more potential occupiers. During the lockdown period, the overall job market declined but the labor requirements of call center firms remained stable. The BPO industry also experienced difficulty in work-from-home scheme due to productivity reasons thus. This signifies bright prospects for flexible office spaces.

Moving forward, the dilemma facing the office market right now is just temporary. Once the business restrictions further ease and more accessible medical solutions have been produced, the demand for office spaces remains an eye for the majority of occupiers. The longevity of the Real Estate Industry will lead to an evolving and resilient new face for the office market.

Figure 3
Metro Manila Office Rents & Vacancy Rates for Q2 2020



Source: Santos Knight Frank Research

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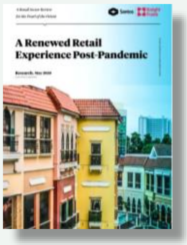

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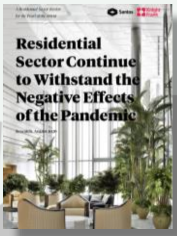

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