Santos | Knight Frank

Philippine Real Estate Outlook 2021

MAPPING THE ROAD AHEAD

Back on the road

2020 was a challenging year for Philippine real estate and the global property market, but we see the new year as a promising time for sectors such as industrial & logistics, office, residential, REITs, and data centers, among others. The industrial & logistics sector was the most stable asset class in the past year, and there are huge opportunities in e-commerce and the rollout of COVID-19 vaccines. The office sector is likely to perform better than 2020, while we anticipate residential real estate to exhibit a slow but gradual rebound.

In 2021, macrotrends such as the boom of e-commerce, flexible office setups, and continued decentralization outside Metro Manila are likely to continue and contribute to the property market's soft recovery.

The Philippine population, which has grown at 1.5% on average each year since 2015, is key to recovery. This growth has created a "demographic sweet spot" and continues to drive consumption and, in particular, the expansion of online retail and the related logistics platforms. The young Philippine population will also continue to keep the country at the forefront of the global BPO industry as outsourcing continues to increase.

2020 was the year of "Work from Home" – while this was clearly a necessity given the restrictions imposed by the pandemic, it also presented multiple challenges for occupiers and their employees here in the Philippines. Data security, the safeguarding of Intellectual Property, internet connectivity, and mental health are among the important issues regularly reported. A gradual return to the office is a priority, and the convergence of commercial and residential strategies will be front of mind for real estate professionals.

On the capital markets front, companies with real estate assets are likely to prioritize liquidity. We anticipate more buying opportunities and a greater volume of deals happening especially in industries negatively impacted by the pandemic, in addition to a move towards non-bank financing and overseas debt and equity funding.

Indeed, while the past year was tumultuous, we see a number of bright spots in the market this year – but getting the right advice is key. *Mapping the Road Ahead: The Philippine Real Estate Outlook 2021* is a collection of insights from Santos Knight Frank and experts across the region, a reflection of our 27-year passion to provide you an end-to-end perspective on property.

We are your **Partners in Property**, and we look forward to helping you navigate this new market environment and chart the road ahead.

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DIVERSIFYING OUTSIDE METRO MANILA

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For the "Secondary Cities" of the Philippines, or those cities outside of the National Capital Region (NCR), the office market in 2021 should continue to look a lot like 2020: Generally soft, but with a few bright spots. Secondary cities will lose one big advantage this year—cost savings—as rents in the NCR continue to fall. But it does not have to be all doom and gloom in 2021, as the COVID-19 pandemic has created a new reason for companies to lease in secondary cities: Viral Diversification.

The BPO industry will be the dominant player in secondary cities, as always. Net leasing growth is estimated at 20,000 to 40,000 sqm in 2021. This growth will mostly come from third-party BPO companies, but a relatively new industry segment—healthcare BPOs—will play a significant role as well. The Fortune 500 BPOs have still largely stayed away from secondary cities, with the exception of Cebu, and that will likely continue to be the case in 2021.

Look for Iloilo to continue its reign as the darling of the secondary cities. Iloilo possesses the attributes that BPOs locators want: Grade A office space, a large hospitality labor pool, scalable city infrastructure, and a secure environment.

Metro Clark and Cebu have most of these attributes too, but they are established areas already. The next wave of cities includes Bacolod and Davao, both of which are being developed, but neither is expected to be on par with Iloilo One bright spot for secondary cities in 2021 could be companies' need to geographically diversify for future pandemics. As seen during the COVID-19 pandemic, the Philippine government is willing to apply different treatments to different regions of the country, depending on the level of pandemic in a given region. For companies, that could mean setting up a secondary office far outside of the NCR—most likely in secondary cities—in order to maintain continuity of their operations in the event of another NCR lockdown. The Philippines has seen similar geographical diversification for the sake of typhoons, earthquakes, and volcanos, but now pandemics can be added to the list as well. ▪

Clark

New infrastructure such as TPLEX and the new airport terminal will enhance accesibility in the region, contributing to the emerging opportunities in the area.

Manila

With office vacancy at 9.8% and asking lease rates having grown by only 1.7% in 2020, the availability of more plug-and-play spaces and prime office space, will be an opportunity for companies aiming for better locations.

Iloilo

The launch of the Batangas-Iloilo-Bacolod shipping route presents opportunities for trade and logistics sector. The residential property market is anticipated to see new supply as developers express intentions to expand

Bacolod

One of the top real estate investment areas outside of Metro Manila. Developers continue to expand their foothold and see potential in the residential market.

Cebu

Ease of restrictions for back-to-office movement provides recovery of small to large retail businesses. The hospitality sector remains optimistic for a gradual recovery in 2021 as domestic travel requirements' ease.

Cagayan de Oro

The city is anticipated to see additional office supply coming from new commercial centers downtown and uptown areas.

Davao

New developments to roll out in 2021. Completion of Davao-Samal bridge to improve trade, logistics, connectivity, and market accessibility.

WHAT WILL THE WORKPLACE LOOK LIKE POST-PANDEMIC?

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To answer the question “What would the workplace look like post COVID-19?”, we need to recognize that the workplace responds to the times and, therefore, pandemic-driven trends will inevitably shape new workplace model and designs in the future.

These days apart from technology and the rising cost of real estate, workplace design is also influenced by human capital. As companies put more value on human capital, organizations have also become more conscious of the multi-generational and multi-cultural workforce that now share the same office space. Ideally, this space should be able to address different needs, wants, and adapt to nuances.

Above all these COVID-19, with its vast effects on health, safety, and costs, has spurred new trends (or revived some) that will impact how we design our workplaces moving forward.

1. Social distancing. Keeping distance of one to two meters is the new norm. Offices and establishments alike cannot accommodate customers at 100% capacity. For companies that are bringing back everyone to the office, this could mean searching for additional space for staff to work in, whether it’s an office extension or seat leasing.

2. Virtual meetings. The increasing concerns and risks of conducting face-to-face meetings mean that the need for meeting rooms will decrease. To utilize space better, existing meeting rooms will be converted as standard workstations or something else that can be more productive than just a vacant space.

3. Digitization or going paperless has been a decades-long campaign and a practice in many companies as it is our social responsibility to reduce our carbon footprint. But because of the pandemic, even paper-reliant companies had to make that switch to go paperless as away to reduce the risk of spreading viruses.

4. Remote working. Even pre-pandemic, this has already become an arrangement for other flexible or non-traditional organizations and companies. As managers and staff become more comfortable and enjoy the benefits of remote working (e.g. cost efficiency, increased productivity, and risk-free of the virus), the more this is seen to extend after the pandemic. Remote working does not necessarily mean working from home. It could be somewhere close home, in a coffee-shop, a co-working space, or wherever you can find your peace and quiet, and work productively and conveniently.

5. Integrated facilities management. Another trend that started, and will persist beyond COVID-19, are new protocols for housekeeping and overall facilities management focusing on sanitation and air quality.

6. Social spaces. Social activities and gatherings have been hampered by social distancing. People and companies have been converting existing social spaces such pantries, game room, and office gym into additional work stations or even storage spaces.

7. Subleasing or shadow spaces. End-users place their fully fitted office space in the market for sublease as a way to reduce operational cost and maximize telecommuting or remote working.

Having seen these trends, we envision that the workplace will evolve from central to dispersed. While organizations typically operated from central headquarters before, the forced experiences and lessons learned during the COVID-19 pandemic made us realize that we need not be physically together to function well—whether as an individual contributor, a team, or the whole organization for that matter. However, because of the value we place on human capital and their development, bringing people together for experience, coaching, and mentoring means that the organization needs to provide the physical space that will support these.

Bringing these two together, the future workplace may likely be a “service offering”—that is, one where the staff can choose where or which venue is best suited for the task at hand. Choices may include the head office/headquarters, the staff’s home, or a facility that is close to home, be it a serviced office or a local café or fast food.

Your organizations’ future workplace will likely be influenced by everything we have mentioned. It is good to know the industry’s best practices, but it is more important to get the pulse of your organization as you craft your way forward. This is the beginning of good change management. ▪

Watch the full interview:

INSIGHTS CORNER
DO WE STILL NEED THE OFFICE?

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Raphael Santos: What happens in an actual physical office can be split into three categories. First is focused work; this is the classic office that means you are going to your desk. Second is collaboration and communication. From quick team meetings to day-long conferences, to a quick cup of coffee in the pantry, you are already collaborating and communicating. Third would be to socialize and revitalize, which have been going around in wellness programs for a lot of companies that is why you have to tackle this as well in a physical office.

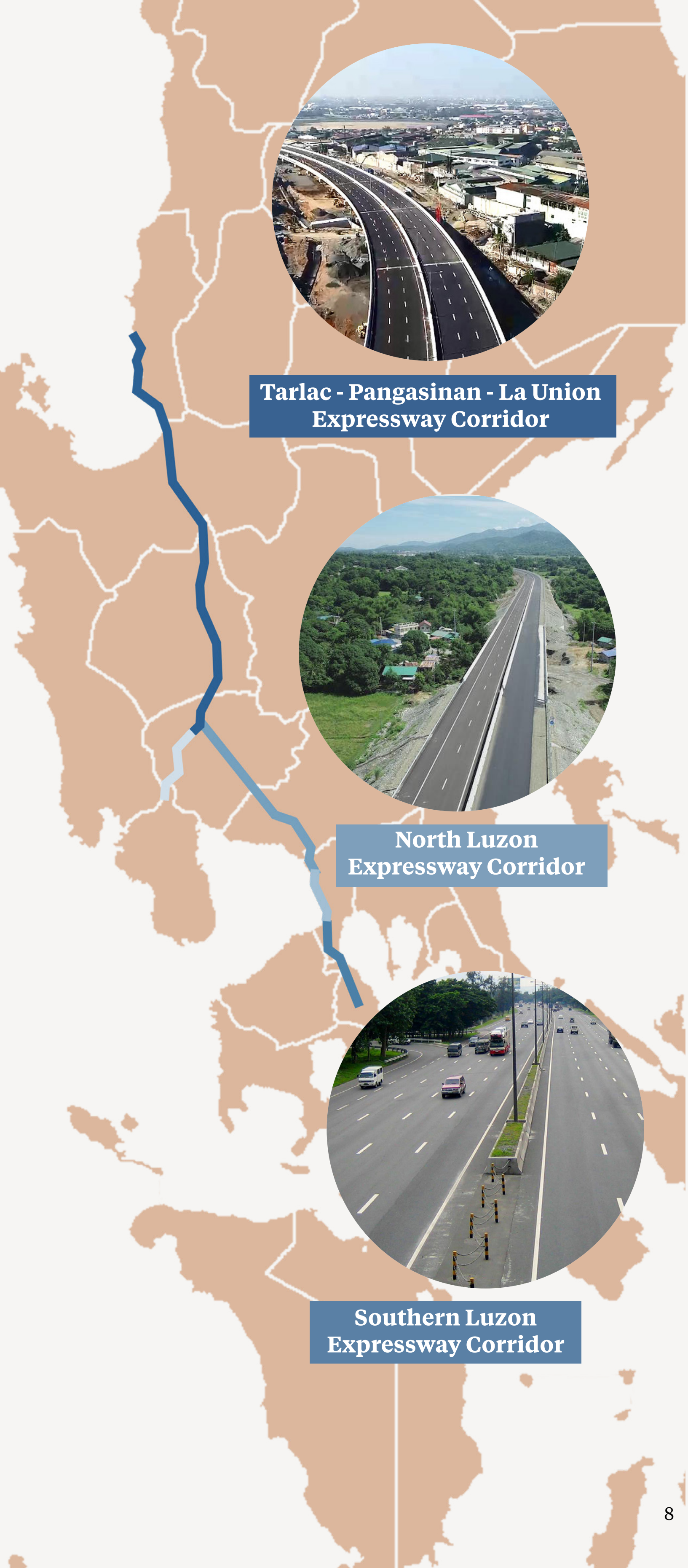
Half of a worker's time is spent on collaborating. That alone is proof that we actually need a physical office. For one, having a physical face-to-face meeting avoids miscommunication. Two, there is emotion in place when you are actually interacting face-to-face. There is so much interaction in a physical face-to-face meeting and actually allows instant feedback. In a typical office when you have workstations back-to-back, you are already having a meeting with your coworker as soon as you turn around. That instant meeting can only happen in a physical office.

Nikki Vergara: It has always been part of our culture that if you work, you go to an office. It is a culture that is really hard to change. It is deeply embedded in our unconscious and it is an obvious basic assumption that everybody who worked had to go to the office. But what this pandemic did was to change our culture. Culture will change after a long history or after a long incident, and pandemic is such a huge critical incident that even conservative work cultures like traditional banks opted to allow their employees to work from home. A lot of people have actually learned during the pandemic that it is possible to work from home. This is the context that frames the question: Given that we can accomplish a lot of work at home, is there still a future for offices? Now let's ask, if people were given the choice, will they actually do all their work from home? Will they choose to work from home all the time? The answer is likely no. Despite the traffic, despite the conveniences of staying at home and having more time with family, a lot of people would still choose to go to the office. There are so many advantages that the physical office gives us.

1. It helps prime our mindset. The physical boundaries actually enforce work-life boundaries. A lot of people are complaining now how tired they are. Many are not able to stop working because there is no separation from the space where they work and where they take care of themselves personally. Without that space and boundary, a lot of workers complain that their mental health and well-being are suffering.

2. The office and seeing each other face-to-face has given us a lot of ways to organically interact with one another and this supports our work. For instance, we measured that members of a particular team felt less competent about the work that they did when they worked remotely. Conversations with a manager helped us understand that it was easier to affirm each other with organic interactions like a pat on the back or a comment of praise when seeing each other in the office. This was harder to do in a remote set-up and the lost confidence was detrimental to work.

Must-watch areas for investment



WHAT'S NEXT FOR INDUSTRIAL & LOGISTICS?

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In 2019 Santos Knight Frank predicted that the industrial and logistics real estate sector will be the next battleground of developers. The unprecedented impact of COVID-19 has accelerated the demand for this sector in real estate further than anticipated.

The viability of this real estate segment proves to be undeniable with the increasing demand for warehousing, cold storage, distribution centers and the likes. driven by e-commerce. The lockdown in the country brought by COVID-19 has forced consumers to adapt and grow more comfortable with e-commerce platforms as part of their daily lives.

Over in 2020 we have seen real estate assets become repurposed. Previous commercial spaces were converted to storage and warehousing facilities. Furthermore, landlords offered competitive rates to gain market share of the growing demand. We think some of the repurposing is temporary given that in the long term, the asset will always be a function of land value.

As such in 2021, we expect a strong and healthy growth in the industrial and logistics segment. This industry is vital in the nationwide rollout of the vaccine against COVID-19. We can expect for the capital market for this industry segment to become more sophisticated. Venture capitalists and investment firms have placed this industry high on their list. In December 2020, CVC Capital announced their partnership with one of the largest logistics companies in our country, Fast Group. The said partnership shows the global readiness of the asset type to be top on of mind when investing in real estate.

INSIGHTS CORNER
LAST-MILE LOGISTICS DURING THE PANDEMIC

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Watch the full interview:

Q: Was the last-mile logistics sector ready for the kind of surge in demand seen over last six months?

Yes in terms of surge in demand, but not so much under the context of COVID-19. We saw disruption in different areas because of the challenges to infrastructure and to the overall ecosystem. The first being our shippers. The lockdown had been a huge problem for businesses, especially those sourcing goods from China, which was one of the first and heaviest-hit markets in the world. The second area is just in terms of whether or not we can meet scale in the market. E-commerce has been growing nominally for the last couple of years. I think logistics and ecommerce have been prepared to keep up with the demand but the shock of changing the ways we operate under the context of COVID has made that especially difficult.

Q: How have you seen consumers' behaviors change? What is this going to mean in terms of expectations for courier services, deliveries, and the future of retail and e-commerce?

I think the first behavioral change came along the retailer—the supply side. The first thing that I have experienced as a consumer was really a problem from restaurants. A lot of restaurants were very hesitant to sell online. But because our malls and retail centers were shut down, restaurants had to make that hard transition online. With that increase in choice of restaurants online, in terms of diversity of products, I think that gave consumers a really powerful reason to buy through ecommerce platforms. I would say that food delivery has been a very profound habit change.

Grocery would be another area that I think was very nascent coming into quarantine. If you recall, early in the quarantine, we were very limited in terms where to buy non-essential goods. The essential goods category was one of those critical industries that made open full out. Grocery was actually one of the first industries that I saw had a high potential, high impact channel.

FIVE TRENDS DRIVING THE RESIDENTIAL SECTOR IN 2021

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Manor by the Sea, Bohol *bit.ly/manorbohol*

How will the effects of COVID-19 loom over the residential real estate market in 2021? Unlike a lot of other real estate sectors, owning a home births from necessity, provided that buyers have the liquidity to match this. Although we are all longing for financial certainty amid the economic downturn, we'll have to look for opportunities and strategies fout of this once-in-a-lifetime occurrence until a vaccine restores consumer confidence and reels in more stability.

Here are some trends that we are currently experiencing and will likely continue to persist in the coming year:

1. Developers and landlords offering flexibility. Property owners have realized the importance of retaining existing buyers and tenants due to the opportunity costs and fixed costs of unsold units and vacancies, especially with an uncertain post-pandemic timeline. A number of developers are offering extended payment terms, lighter down payment schemes, and waived reservation fees with a limited time offers, which financially prepared buyers should take advantage of. Some landlords are also offering either discounts ranging from 5% to 13% for existing tenants or offering friendlier terms of payment in parallel with the grace period offered by banks during the lockdown.

2. Increasing listings in the resale market. Buyers are in better position to search for attractive financial opportunities due to the increase in the number of resale options available in the market. While a number of sellers are still on a wait-and-see mode before deciding to adjust prices, those sellers who prioritize liquidating within the short-term of one to two years should take pricing and research more seriously and realistically. Meanwhile, liquid buyers may encounter rare investment opportunities with proper research and professional help.

3. Condominium vacancies in POGO-occupied segments. The restrictions in travel have made it seemingly impossible to absorb further residential demand from POGOs Areas that were once priced for POGO demand should. expect price reductions to alleviate slower take up, while travel restrictions are in place worldwide. While we expect arrivals from non-POGO sectors, or from expatriates with travel ban exemptions, to slowly increase by the first half of 2021, the intensity of take up will likely be subdued in the short term.

4. Accelerated pace to digitization, but.... The real estate segment has been a relatively slow runner in keeping p with e-commerce. There is a human element in real estate that is essential in the buying process. However, more sellers have been forced to go digital especially during the three-month lockdown. Developers have also offered virtual 360-degree showrooms. Despite this, the human connection is much more valuable in terms of providing the right advice to buyers and sellers, to sift opportunities out of the muddle of information online.

> **"There is a human element in real estate that is essential in the buying process."**

5. Acquisition of homes in low-density areas. With the safe haven of living in low density and the much sought-after idyllic environment, houses in the provinces near Metro Manila, especially beach homes, continue to attract the wealthy. Developers have also experienced higher post-lockdown activity for upscale subdivisions in provincial areas close to Metro Manila.

"As 2021 unfolds, more businesses in both commercial and real estate sectors are adapting sustainable design as a 'must-have,' rather than 'nice-to-have.' "

Image Source: Unsplash

THE FUTURE OF SUSTAINABLE BUILDINGS

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The world has been deeply shaken by the numerous challenges happened in the year 2020. Pandemic restrictions, bankruptcy, and unemployment are among the top challenges that impacted society the most. Widespread economic recession occurred in global scale. Aside from these disturbances, prevalent environmental and social concerns are being considered to become integral in counteracting economic issues—all to be part of the triple bottom line paradigm.

As sustainable building technologies advance at monumental pace, building architects, engineers, and developers around the world are offering progressively innovative interpretations of sustainable trends. Green design and Best Management Practices (BMPs) are leading the edge with comprehensive building philosophies that go beyond LEED (Leadership in Energy and Environmental Design certification system) and other green certifications to answer fundamental questions about how and why we build responsibly. With aiming for the future of sustainable buildings, we continuously aspire in making eco-friendly structures and establishments.

Here are the four directions of sustainable buildings in the future:

1. Net Zero Energy. The strategy of consuming a total amount of building annual energy that is equal to the amount of renewable energy created on the site. Energy-efficient building envelope and equipment utility systems are key elements of a net zero energy building.

2. Net Zero Water. Designed to minimize total water consumption, maximize alternative water sources, and minimize wastewater discharge from the building and return water to the original water source. It creates a water-neutral building where the amount of alternative water used and water returned to the original water source is equal to the building's total water consumption. The goal of net zero water is to preserve the quantity and quality of natural water resources with minimal deterioration, depletion, and rerouting of water by utilizing potential alternative water sources and water efficiency measures to minimize the use of supplied freshwater.

3. Net Zero Waste. The conservation of all resources by means of responsible production, consumption, reuse, and recovery of all products, packaging, and materials, without burning them, and without discharges to land, water, or air that threaten the environment or human health. Achieving Net Zero Waste means reducing, reusing, and recovering waste streams to convert them to valuable resources with zero solid waste sent to landfills over the course of the year.

4. Advancement of Green Building Rating System. LEED is the world's leading green building project and performance management system, delivering a comprehensive framework for green building design, construction, operations and performance. Adapting to global challenges and continuously evolving the needs of present society, LEED v4.1 raises the bar on building standards to address energy efficiency, water conservation, site selection and management, material resource efficiency, day lighting and waste reduction. Other green rating systems such as EDGE, WELL, and Green Globes contribute supplementary information on addressing specific green building metrics.

As 2021 unfolds, more businesses in both commercial and real estate sectors are adapting sustainable design as a "must-have," rather than "nice-to-have". This is its most important lesson: allowing us the insight, strength, and compassion to build a sustainable, resilient and robust future. Investments in low carbon development, including building sustainable infrastructure and improving energy efficiency, could both accelerate economic recovery and promote long-term sustainable growth. (*With insights from Eric Bautista.*) ▪

PROPERTY MANAGEMENT: WHY RESILIENCY IS KEY

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In preparation for 2021, I have been discussing the importance for property managers to work on their building resiliency strategy based on the pillars of CPR: Communication, Preparation, and Response. This strategy is long-term and it should evolve together with the property management operation. There is a need to continuously review, revise, and improve existing business continuity plans. This pandemic is making a strong and lasting impact on the property management profession and it has effectively forced real estate companies to alter their operational strategies.

The COVID-19 pandemic has given the property management industry the chance to reflect and accelerate the utilization of resources in the implementation of new approaches during the "New Normal". Before the pandemic, most buildings, specifically residential condominiums, have been constrained in using smart building technology because of cost and budget limitations. What we've seen now is more building developers and residents reaching into their financial investing to adopt new technologies that enable more efficient property and facilities management and help support a safe and healthy environment.

With a smart building technology, it would be easier now to manage building population or density, track potential COVID-19 exposure, and effectively manage the building equipment including sanitation, airflow, and lighting. It also would lessen face-to-face interaction because it can cover reservation systems and tenancy and guest management.

The focus of property managers in 2021 will be the implementation of health and safety protocols; maintaining revenue by increasing or stabilizing the occupancy of properties; and providing the best customer experience for all residents, tenants, and guests so that they see the value of their rents and dues. Cash is king especially during uncertain times. Property managers are expected to pivot, manage their operational expenses, and set priorities on spending.

Professional property management services will be the stabilizer and lifeblood of the real estate industry. More developers and building owners will realize the importance of having professional property managers especially during challenging times. Technology will play a major part in solving most of property management problems. There will also be a major boost on the use of property management software. Property management services will take a major role in shaping up and influencing the landscape of the real estate industry in adherence to health and safety of its communities. ▪

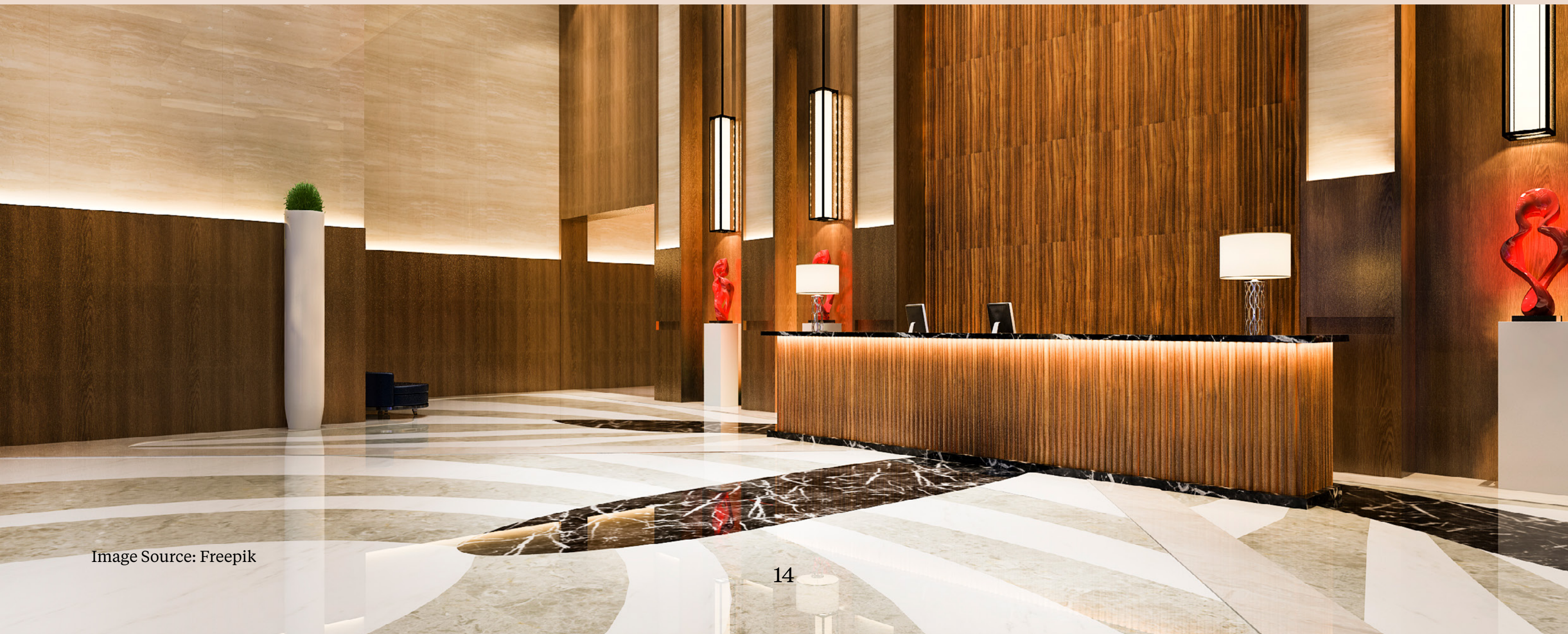

Image Source: Freepik

WE SHOULD TALK MORE ABOUT INDOOR AIR QUALITY IN 2021

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Air quality, which basically specifies the cleanliness of air, has long been a critical issue among building owners and occupiers – but it has only been now that the world's attention has focused on indoor air because of the ways COVID-19 is spread. Organizations such as the American Society of Heating, Refrigerating and Air-Conditioning Engineers (ASHRAE), the World Health Organization (WHO), and Center for Disease Control have long been educating the world about the importance of good air quality, especially in closed areas such as buildings and transportation. Research have given birth for applications and standards for indoor air quality (IAQ).

IAQ refers to the types of concentrations of contaminants in indoor air that are known or suspected to affect people's comfort, wellbeing, health, learning outcomes, and work performance. In short, it refers to the fresh air amount in a closed area. Think about it: Every day we use our heating, ventilation, and air-conditioning (HVAC) systems or air conditioning systems, which get fresh air from the outside, filters, cools it and supplies into our zone. Outside air potentially contains biological and non-biological particles, pathogens, and organic and inorganic gasses. Many reports and studies indicate that children, elderly, low-income, minority, and indigenous people are disproportionately impacted by indoor air. Indoor air may also trigger asthma attacks, cause short breathing, and other sicknesses.

Beyond wellbeing of occupants, there are more reasons why greater attention should be devoted on IAQ. Looking at IAQ also means examining the facility's or building's energy efficiency – a major cost in operations. IAQ processes are related with a facility's HVAC or HVAC-refrigeration and filtration systems, maintenance frequencies and methodologies, and monitoring systems.

Lastly, IAQ ensures fresh air inside one's life zone through proper ventilation and the removal of dirty and exhaust air. The importance of IAQ has been pointed out by many HVAC experts and standard organizations such as WHO, ASHREA, LEED, and the Air Conditioning Contractors of America.

How do we improve IAQ in properties this 2021 and beyond? Here are four ways.

1. **Increase air circulation and outdoor air.** Technicians can measure and possibly even adjust the amount of outdoor air coming into the building and increase ventilation. bring fresher air flow, increase the ventilation air and air circulation. For better filtration, consider redesigning your HVAC or HVAC\R systems. Circulate more fresh air in non-medical buildings and increase the filtration. For medical buildings, improve ventilation and filtration systems.

2. **Think green.** We need to acknowledge the negative impact to respiratory health that so many materials and products. Reduce toxic indoor contaminants. Consider implementing policies for the use of greener cleaning products, integrated pest management systems that use fewer toxic chemicals, and low-emitting paints and sealants. In addition, choose naturally-breathing, low-carbon construction materials for an organic temperature in an indoor environment. Plant trees as much as possible to reduce the need for air-conditioning in the building.

3. **Good maintenance.** Increase your maintenance activities and due diligence by making sure building maintenance personnel practice IAQ and testing, adjusting and balancing (TAB) to help make the building environment healthier, safer, and more comfortable to work and live in. Give your building ventilation system a regular tune up that increases fresh air and air flow. Change the filters, especially outdoor filters. Outdoor air includes many particles and pathogens.

4. **Invest in better technology.** Replace old units. Many older buildings were not designed with ventilation systems that meet even today's minimum standards. A new retrofit for older buildings can achieve a new ventilation system that is up to current standards for modern buildings. If your building is unoccupied at the moment, it is a great time to be changing out equipment without disrupting work flow.

OPPORTUNITIES FOR INVESTORS IN 2021: AN ASIA PACIFIC PERSPECTIVE

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Watch the full interview:

The COVID-19 outbreak has upended expectations, shifted investment strategies and forced investors to rethink their priorities. In 2021, as Asia-Pacific and the world at large emerge from the pandemic's shadow, we discuss some strategies and areas of opportunities for investors targeting this region.

The Asia-Pacific outlook

The economic impact of COVID-19 has, to date, been less extreme in many major Asian markets compared to the West. Bolstered by strong domestic demand, commercial property transactions in South Korea and the Chinese Mainland remained stable throughout 2020 – though markets reliant on cross-border transactions such as Hong Kong SAR and Singapore witnessed a more drastic fall as lockdowns impeded liquidity. In the Philippines, companies low in liquidity are looking to sell capital assets to support business operations. With the development and rollout of the vaccine, there is consensus that Asia-Pacific markets will see a measure of recovery in 2021.

However, this will be uneven across the region due to logistical challenges around transporting the vaccine, thereby deepening the divergence in geographical and sectoral performance in 2021.

Sectors

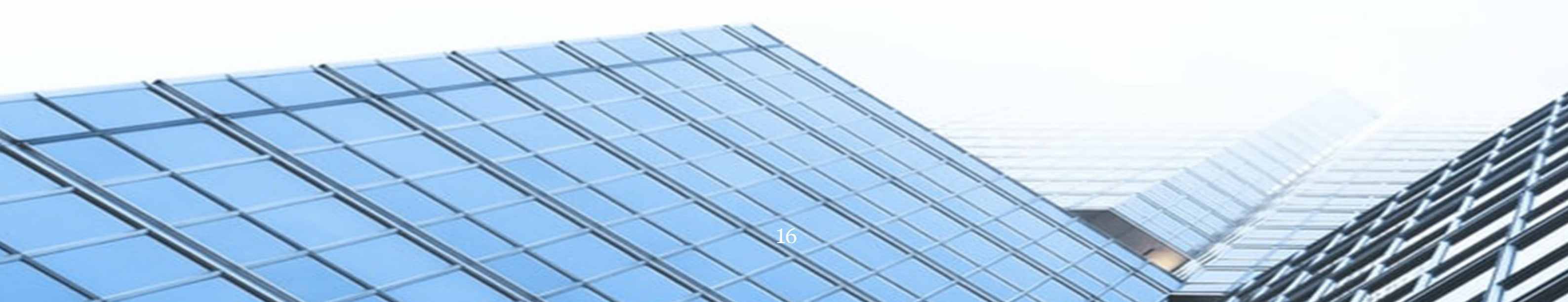
As we discussed in our Active Capital research, the notion of positioning for resilience remains at the heart of any investment decision. In Asia-Pacific, core, well-let commercial assets with long-term income prospects continue to be in demand.

Some pundits have questioned the strength of occupier demand, though offices are far from facing an existential threat, even if the way we work has irrevocably changed. The office sector will continue to play a prominent role in portfolio allocations: in 2020, offices attracted 47% of all transaction volumes within Asia-Pacific.

Assets best placed to weather shocks and benefit from the recovery and broader structural changes have seen a similar surge in interest, with industrial, warehousing and data centres proving to be the biggest winners – this is true even in the Philippines, which is likely to continue seeing stronger inflow of capital for logistics and warehousing. Across Asia-Pacific, the market share for industrial assets has increased by more than 50% of market share compared to its historical five-year average.

Intra-regional investment

Recovery to pre-Covid volumes may not happen soon, but capital flows between liquid and trusted global safe-havens will continue. For investors, cross-border property investments offers true diversification and more options to meet revenue targets. In a period where physical travel remains subject to restrictions, intra-regional investment into 'near neighbour' locations will become ever more compelling, with investors from Singapore and Hong Kong SAR, stepping up investment into the Chinese Mainland. ■



INSIGHTS CORNER
REITs IN ASIA PACIFIC

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Watch the full interview:

Q: 2019 was a great year for REITs but they were pummeled in 2020. Are investors buying on dips or are they shifting to specialist practices such as data centers, healthcare, and industrial and logistics?

REITs have not been spared from the volatility that we have seen in the equities market. REITs have had double digit returns, historically. We were looking around 20% in terms of returns across all assets—including office, retail, hospitality, and hot new classes like data centers, logistics, and so on—before COVID-19 caused a short selloff. We have seen some of the REITs conserve cash and cut back on some of the distribution per unit, but this is really not a story across the board. Fortunately, the markets have also stabilized so we've seen the REIT market recover, recoup some losses (about 15% up from their March lows), with credit given to governments for helping us out. On a sector level, sectors like data centers and logistics are very popular among investors. And this is a story that has been playing out before the pandemic. What the pandemic has done was really to accelerate investors' interests towards these sectors.

Q: What is your outlook for REITs in Asia-Pacific especially in the Philippines? Do you see more REITs coming to the market?

Yes, and there are many reasons why. For investors, returns from REITs are very good at over 10-15%. REITS also provide liquidity. At the same time, REITs can benefit from government support, just like in China and India. Their REITs are largely focused on infrastructure which we all know is critical for urbanization and economic growth. For the Philippines, economic significance is also there. Philippine REITs tend to focus on the office sector. That's key because the BPO sector contributes significantly to the country's economy. For the BPO sector to thrive, real estate has to support that.

WHAT IS THE POTENTIAL GROWTH FOR SOUTHEAST ASIA'S DATA CENTER SECTOR OVER THE COMING DECADE?

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Watch the full interview:

What are some of the main drivers?

With the exception of Singapore, the data center market in Southeast Asia is still in its infancy. Many emerging economies within the region lack the minimum infrastructure required for the sector to function (e.g. stable power supply, extensive fibre broadband network etc.). Despite these challenges, the potential opportunities from establishing a healthy data centre industry within these economies far outweighs the risks. The region's middle-class is forecast to expand rapidly which will not only accelerate e-commerce growth, but also drive a greater amount of data consumption and data generation.

Cybersecurity concerns are another driver of data center growth within Southeast Asia. Local and government-linked enterprises, which contribute a large proportion to local economies, will increasingly need data centre services. Due to national security concerns, governments across the region would prefer to see data stored and processed domestically rather than relying on major data centers outside their territory.

What could growth look like?

Analysis of the current capacity of Southeast Asian markets compared to the largest data centre markets within the Asia-Pacific region, underlines the potential for growth.

	Market	Capacity (MW)*	City Population	MW per mn
Developed Markets	Tokyo	300	37.4	8.0
	Seoul	200	10.0	20.1
	Shanghai	250	27.1	9.2
	Beijing	300	20.5	14.7
	Hong Kong	370	7.5	49.0
	Singapore	400	5.9	67.4
	Sydney	400	4.9	81.2
	Average			35.7
	Average (ex. SG)			**30.4**
SEA Markets	Bangkok	25	10.5	2.4
	Manila	20	13.9	1.4
	Vietnam (HCMC/ Hanoi)	15	13.3	1.1
	Kuala Lumpur	40	8.0	5.0
	Jakarta	60	10.8	5.6
	Average			**3.1**

Source: Knight Frank Research *estimates as at end-2019

From the table, the major Asia-Pacific data centre markets have a current capacity of 35.7 MW per million capita (taking into consideration only the city population) as at the end of 2019. If we were to exclude Singapore, which currently acts as the data center hub for Southeast Asia, the per capita rate falls to 30.4 MW per million. This is almost tenfold the current capacity per capita for the Southeast Asian markets which have on average only 3.1 MW per million capita.

Market	MW Per mn	10YR CAGR
Developed Peers	30.4	
SEA Average	3.1	26%
Bangkok	2.4	29%
Manila	1.4	36%
Vietnam (HCMC + Hanoi)	1.1	39%
Kuala Lumpur	5.0	20%
Jakarta	5.6	18%

Source: Knight Frank Research *estimates as at end-2019

Now if we assume that the Southeast Asian markets, at their current 3.1 MW per million capita average, play catch-up with their Asia-Pacific developed peers over a 10-year period, given that infrastructure will take some time to plan and construct, this equates to an annual CAGR of around 26%. Taking a closer look at the data, Manila and Vietnam (HCMC and Hanoi) stand out as two markets that are projected to be the fastest growing with 10-year CAGRs of 36% and 39% respectively. Furthermore, we must note that our growth estimates are on the conservative side as our calculations have yet to factor in population growth which will increase our CAGR calculations.

Next Steps?

Southeast Asia is expected to be a bright spot for data center growth within Asia-Pacific as the region's data center industry (excluding Singapore) remains relatively undeveloped. But with its growing middle-class demographic and the subsequent boom in technology and data consumption, it will be a region that investors, occupiers, and solution providers find hard to ignore. Granted there are risks involved and an immature infrastructure environment is currently not able to support rapid growth, but this should change over the longer term as governments have acknowledged and are largely expected to steadily improve their technology infrastructure over the coming decade.

THE FINAL WORD

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The past year saw the COVID-19 pandemic bringing an unparalleled challenge which cut across all sectors on a global scale. Most, if not all, countries experienced major setbacks such as closure of businesses, loss of jobs and more tragically, loss of lives. However, like all challenges, this too will come to pass. The Philippines is no stranger to natural calamities and has always shown resilience in the face of adversity.

The pandemic was a rude awakening as it made us realize how we took a lot of the simple and basic things for granted. On a personal level, simple hand washing and practicing proper sanitation and hygiene was often neglected. On the level of buildings and similar facilities, proper ventilation, adequate open spaces and proper upkeeping practices were more of a “good to have” instead of a “must have”. Getting these things and practices done will be a part of the basic routine as we transition to the “new normal”.

Working from home, to some extent, will be part of the “new normal” in this period of pandemic. The requirement to practice “social distancing” has limited the number of people in certain locations at one time, especially in the office. Some employees were required to physically report to the office everyday. Others were required to report for work at regular intervals (e.g. one week in the office then one week at home, etc.). While some were to virtually report for work (i.e. work from home, work remotely outside the office).

While working from home may prove effective for some industries, working in the office would still be indispensable to others. Changes in the workplace need to be introduced and applied to address the requirement to practice “social distancing”. Being able to work efficiently in the office while adhering to the strict guidelines in place would require physical changes to the office itself and for the people working in them to adapt to these changes. Humans by nature are “social animals”. The need to physically interact in a physical environment, such as the office, will still remain in the foreseeable future.

Opportunities have also risen over the past year. The lockdown experienced during the enhanced community quarantine (ECQ) highlighted the need to diversify to key locations outside of Metro Manila. The economy and the general public suffered severely as most of the activity which was centered in Metro Manila, were halted during the lockdown. In addition, Metro Manila was one of the areas which remained under ECQ the longest which made the situation worse. Diversifying to locations outside of Metro Manila will spread these activities and lessen the occurrences of disruptions on these whether by forces of nature (e.g. typhoons, earthquakes, volcanic eruptions, pandemic) or man-made events (e.g. protests, riots, demonstrations).
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Other opportunities have been around for quite some time but the need for them has been accelerated because of increased demand for some of the activities that they are able to service. Such has been the case with industrial and logistics property as well as data centers with the expansion of online transactions. Transacting online has decreased physical contact significantly and has been effective in reducing the transmission of the virus.

The REIT has been one of the more recent opportunities that have risen and is currently showing success with the performance of the AREIT, the lone REIT in the market today. Other developers may soon follow suit and hopefully the capital to be generated may be used fund new developments and jumpstart the real estate market and other related industries.

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