Metro Manila Office Market Update

Introduction of office supply adjusted further due to changing restrictions

Q3 2021

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General Overview

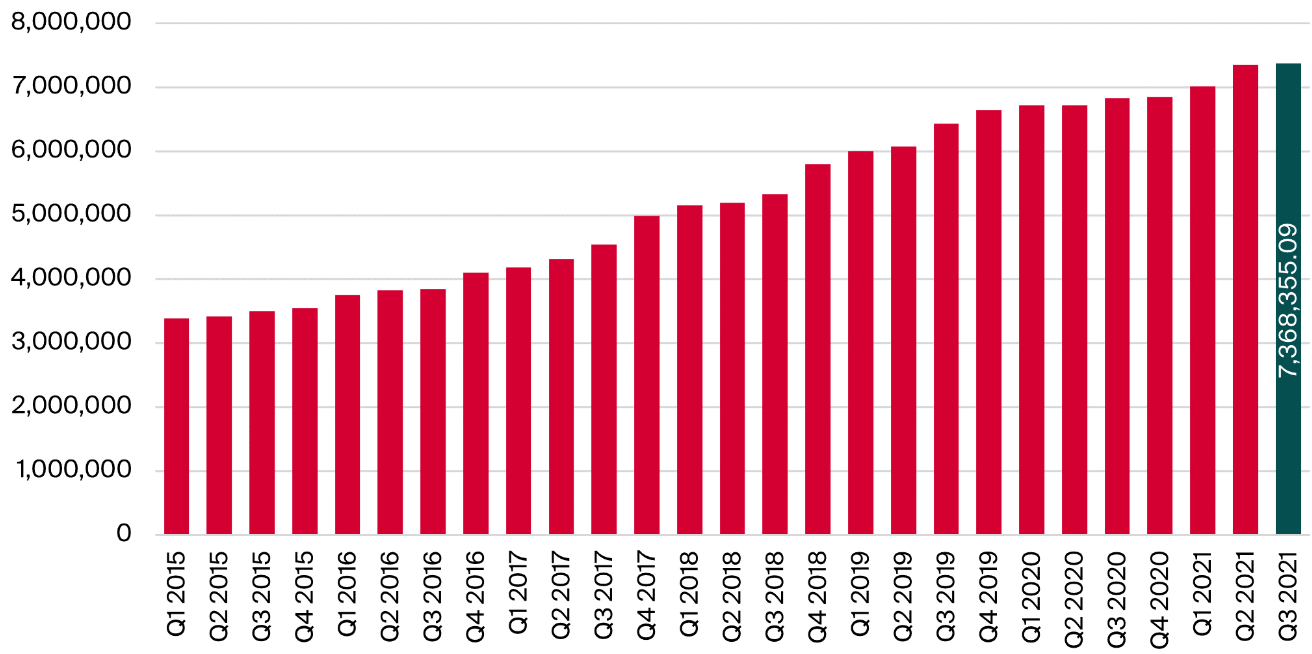
The Metro Manila office market experienced a slowdown in Q3 2021 amid the new wave of COVID-19 cases. Stricter quarantine measures were again implemented in Metro Manila impeding the economic momentum that was experienced in the preceding months. Landlords were again challenged as these protocols influenced the decision-making process of some potential locators considering taking up an office space.

Albeit the changing scenario, new office buildings were still completed in the market during the quarter. The office supply grew by 21,624 sqm which came from Grade A projects that were mostly situated in Quezon City and Alabang. This has pushed the overall office supply in Metro Manila to 7,368,355 sqm.

As a result of the supply growth during the quarter, vacancies increased throughout the metropolis. As of Q3 2021, the office vacancy rate rose to 18.58%, the highest in the past ten years. The mass exit in the offshore gaming industry and the extension of work-from-home arrangements for up to 90% in the IT-BPO industries were also attributed to the increased vacancy. An additional 57,000 sqm of office spaces were freed up during the quarter pushing the total vacancy to around 1.37 million sqm. Several locators have continued downsizing their spaces to minimize their operating costs. Simultaneously, some developers were also keen on repurposing their office facilities.

The average asking lease rates in Metro Manila dipped to PHP 1,095.41 per sqm per month, contracting by 0.42% quarter-on-quarter (q-o-q), and 1.32% year-on-year (y-o-y). The contraction was attributed to the landlords' urgency to heed the calls of current and potential locators on lease considerations amid the tight competition in the office market.

Figure 1. Historical Office Supply in Metro Manila



Source: Santos Knight Frank Research

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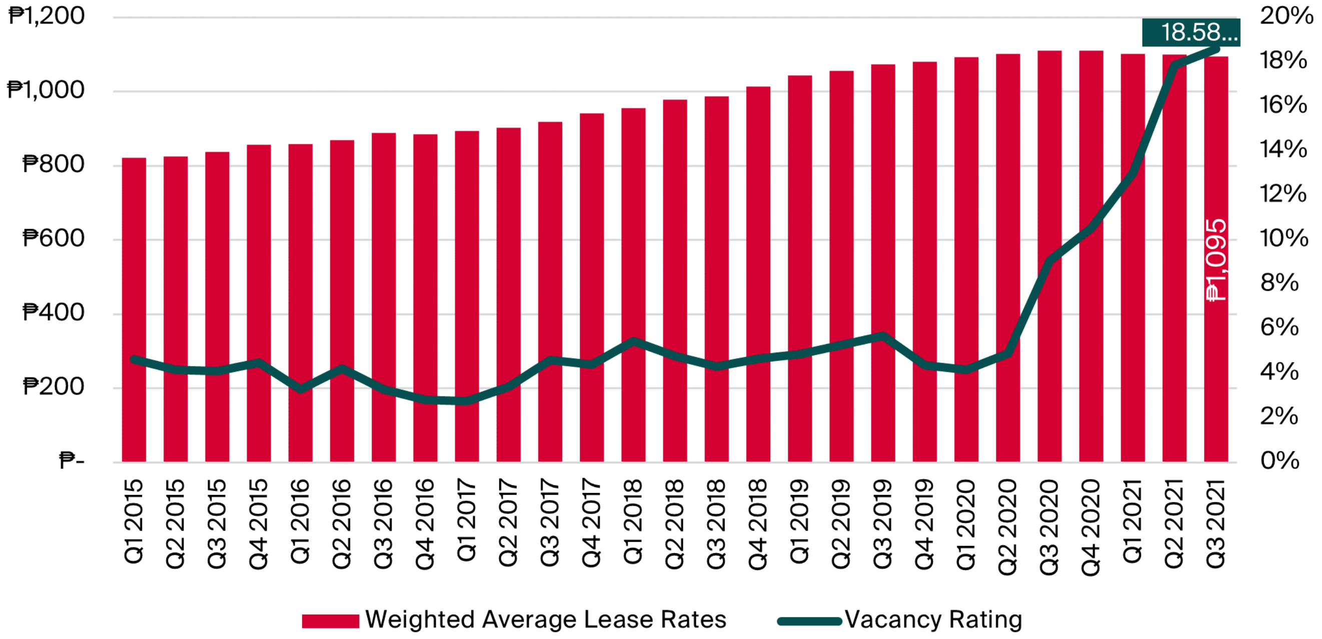
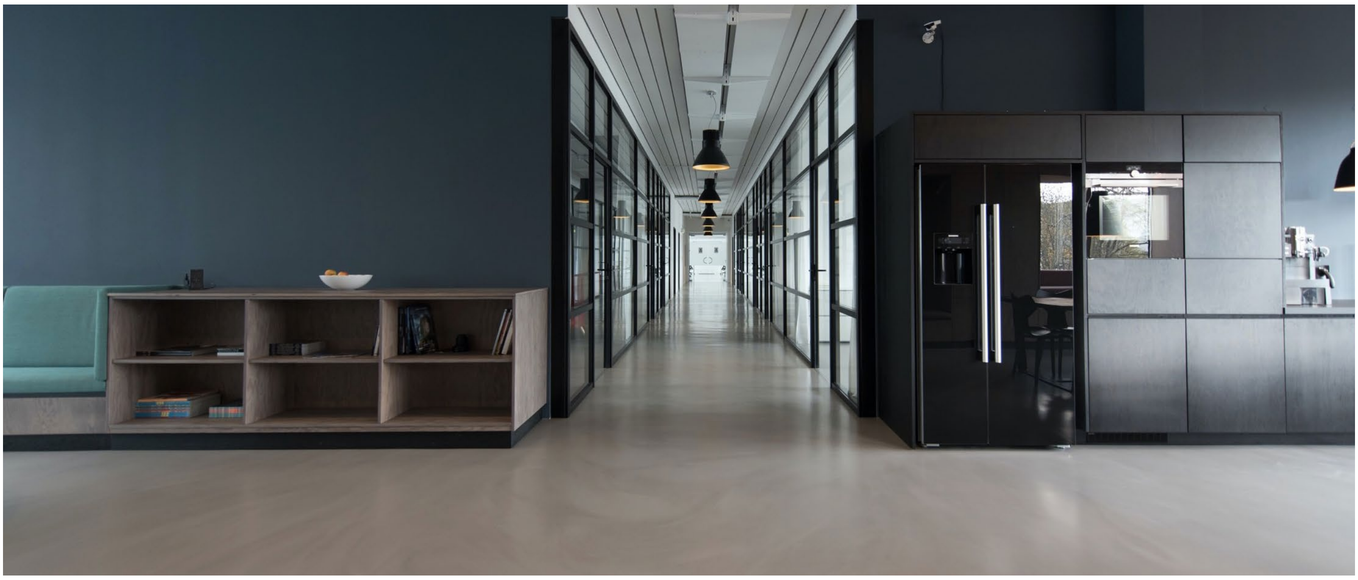
Figure 2. Metro Manila Historical Lease & Vacancy Rates



Source: Santos Knight Frank Research

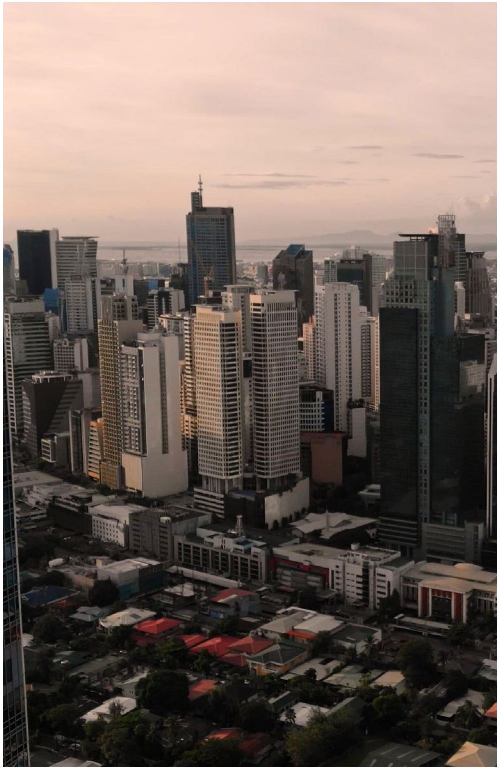


Makati

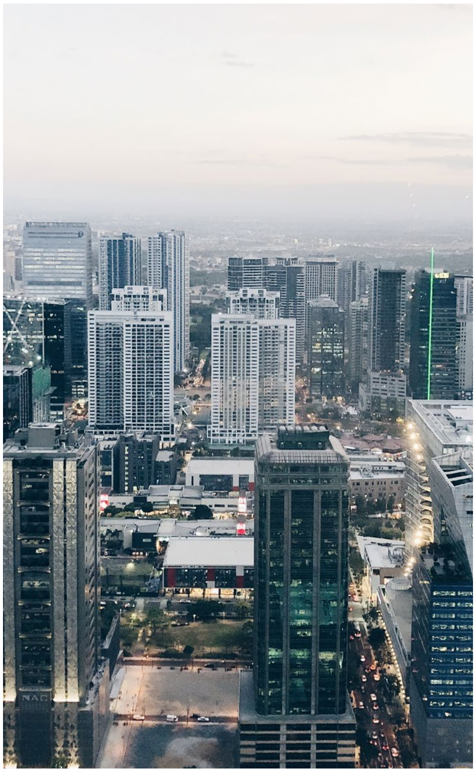
The slowdown in demand persisted in the most prominent district in the country during the quarter. Vacancy rates rose to 17.41%, the highest for the past ten years. Potential tenants were still in the process of reassessing their need for office spaces, causing delays in their occupancy plans. Furthermore, more tenants have vacated their premises during the period causing a negative net absorption of 36,134 sqm.

Albeit the sluggish demand, Makati continued to command the highest asking rental rates in Metro Manila. The average asking rental rates were recorded at PHP 1,341.01 per sqm per month. Prevailing asking rates in the area have even increased by 0.22% q-o-q with landlords speculating towards the recovery of the market.

In the succeeding years, office activity in Makati CBD is seen to pick up with its upcoming developments. Several property players are still keen on pushing through with their office developments in the pipeline. More than 496,000 sqm of newly constructed Prime and Grade A offices are expected to become available in the next three years, in which 157,000 sqm are anticipated to be operational by the end of 2021.



Fort Bonifacio



Fort Bonifacio has shown signs of recovery during the quarter as the vacancy rates slightly eased to 11.25%. The absence of POGO companies in the district has cushioned it from a greater surge in vacancies that was witnessed in other business districts. Like Makati, landlords had bright prospects towards the market especially with the improvement in the vacancies. As such, the average asking rents in the area rose to PHP 1,271.17 sqm per month, increasing by 0.34% q-o-q..

Moreover, the competitive environment in the area has been beneficial to its office market as it remained the sought-after address by both multinational and local companies. In line with this, the Prime and Grade A office supply is expected to be augmented by about 547,000 sqm within the next five years. Additionally, about 344, 000 sqm of space shall also be introduced in the neighboring Arca South, a master-planned community development that is poised to become a new business district.

Bay Area

The inactivity of the POGO industry has remained evident in the Bay Area. The tightened regulations and income tax imposed concerning the operations of POGOs have been detrimental to office landlords. Slow demand from the sector persisted and has pushed average rental rates went down by PHP 1,119.29 per sqm per month, contracting by 3.64% q-o-q. However, the general condition has slightly improved as the aggregate vacancy rating inched up by 0.71 percentage points to 23.27% from its value in the preceding quarter.

Despite the slowdown in demand, several property players are still keen to invest in the district due to its accessibility and availability of developable land. Seeing this opportunity, a huge amount of upcoming office supply is still expected in the district in the coming years. Approximately, 619,475 sqm of spaces are anticipated to be introduced in the next five years- 181,996 sqm are expected to become operational by the end of 2021.

Ortigas Center

Ortigas Center recorded the highest office vacancy in Metro Manila during Q3 2021. Vacancy rate was recorded at 25.57%, due to the surge of newly built spaces that are yet to be absorbed by the market. The cutthroat competition among these high-quality offices has elicited a price war during the quarter. As such, the average asking rents went down to PHP 828.49 per sqm per month, contracting by 1.03% q-o-q.

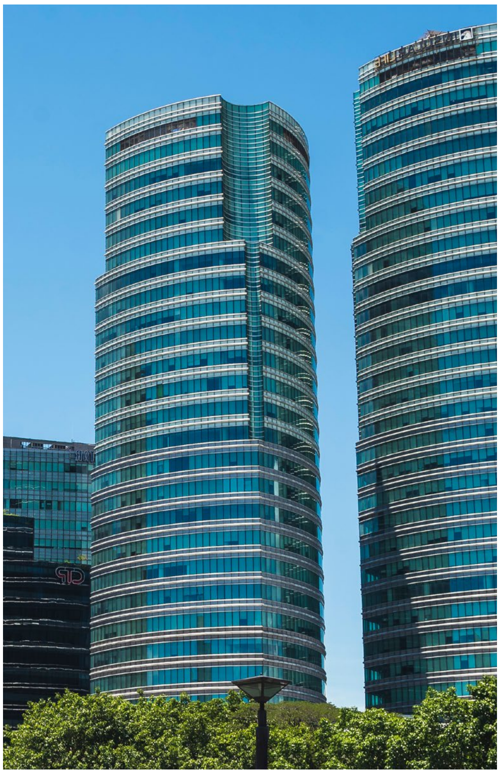
Several property players are still looking forward to the materialization of their projects in the pipeline. Ortigas Center is still expecting a significant boost in supply in the upcoming years. Approximately, 549,125 sqm is anticipated to become operational in the next five years, while 158,004 sqm will be operational by the end of 2021. The massive influx of upcoming office developments in Ortigas comes from delayed projects due to the pandemic.

Quezon City

The slow demand in Quezon City was also evident as the vacancy rates increased to 19.33% from 17.47% of the preceding quarter. This upsurge was mainly attributed to the slow office take-up and the completion of SM Fairview Tower 4 that added 13,000 sqm to the overall office supply of the area. Approximately 11,065 sqm were freed up in the district during the period. Additionally, the newly completed offices in the city have also helped in pushing the average rents in the area to PHP 932.23 per sqm per month, increasing by 2.74% q-o-q.

Numerous pocket developments continue to spur in Quezon City as developers view to increase their property footprint in the metropolis. This has caused a higher upcoming office supply in the area. More than 547,605 sqm of Prime and Grade A offices are slated to be introduced within the next five years, while 62,868 sqm are expected to become operational by the end of 2021.

Alabang

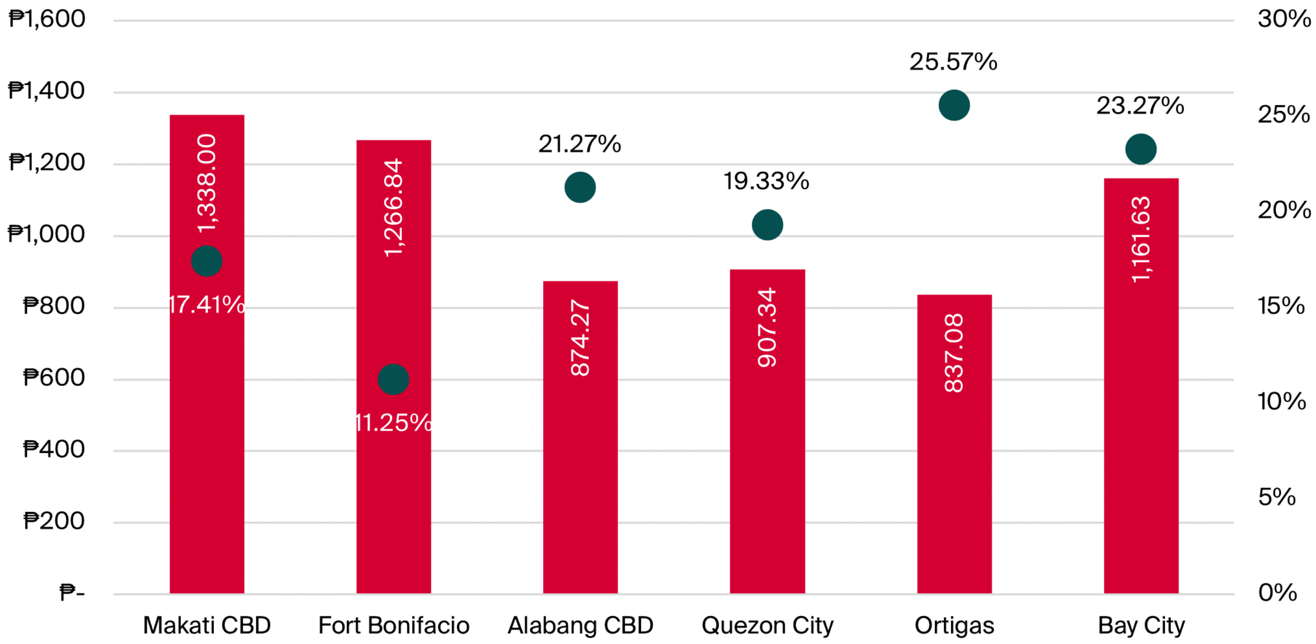


The vacancy rates in Alabang spiked up to 21.27% from 19.30% of the preceding quarter. The contraction in office demand was attributed to lease cancellations from potential locators and existing tenants that mostly came from IT-BPO companies due to the extension of work-from-home arrangements. Similar to other districts, new projects in the area have contributed to the rising vacancies. Notably, Southkey Hub 2 came online during the quarter with an additional 7,843 sqm of Grade A offices.

This vacancy trend has influenced the decreasing rental rates in Alabang during the quarter. Landlords tried to alleviate this downtrend and are still vying to mitigate lease terminations. As a result, the average asking rents went down to PHP 843.00 per sqm per month, contracting by 3.49% q-o-q.

Moreover, Alabang still holds on to the possibility of becoming one of the major investment hubs in Metro Manila due to the improvements in the accessibility and connectivity from the completed and ongoing road projects. At present, 228,835 sqm of upcoming office supply is anticipated to come online within the next five years. This figure might further be augmented as investment appetite recovers from the pandemic.

Figure 3. Metro Manila Lease and Vacancy Rates per CBD

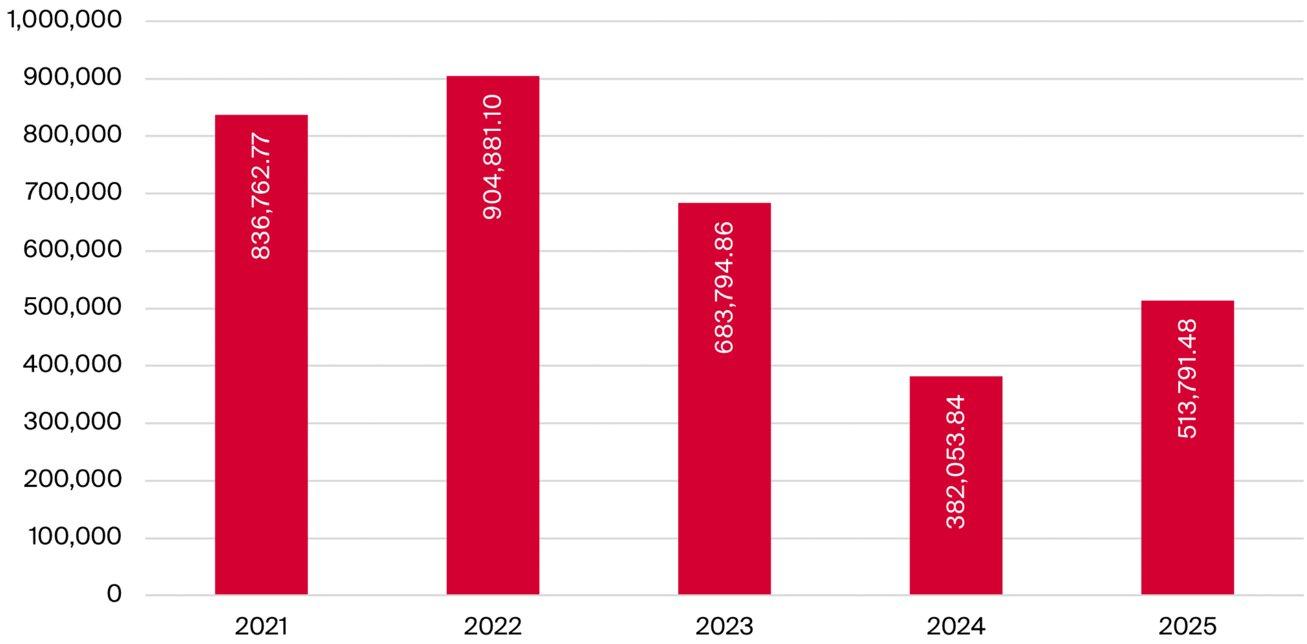


Source: Santos Knight Frank Research

Office Outlook

The implementation of stricter lockdown systems during the third quarter of 2021 has urged property developers to take a cautious approach in the introduction of new office developments. The current surplus in supply has been pushing the vacancy levels higher. This trend is anticipated to persist in the next few quarters as the Metro Manila office market is slated to see an additional supply of 836,000 sqm by the end of the year. This figure is even lower than the expected completion as most of the upcoming offices were delayed due to the pandemic.

Figure 4. Metro Manila Office Pipeline (Q4 2021 to 2025)



Source: Santos Knight Frank Research

Property developers are also expected to increase their stakes into the Real Estate Investment Trust (REIT) market as a means to augment their working capital. In turn, investors are enticed in the alternative investment option on the property market as they diversify their respective portfolios.

The weakened office demand is seen to continue in the coming quarters due to the extension of PEZA provision on the IT-BPO sector. The downward trend of rental rates and occupancy would still persist as potential locators will still remain cautious and will carefully evaluate expansion plans as they wait for market conditions to improve. Office landlords are expected to keep on implementing flexible payment terms to retain existing and attract potential tenants to secure continuous cash flow from their buildings.

Green shoots in the office market are coming from from pandemic-resilient industries that include healthcare, insurance, and tech companies. Demand from these firms was driven by the continuous operations amidst changing quarantine restrictions. Recovery and growth prospects from outsourcing and shared service companies are expected to gradually take up the surplus in the office market.

Stronger demand for green buildings is also anticipated to materialize in the medium to long term as potential locators will be more inclined to take up spaces in these kinds of projects either dictated as a global mandate or by its own initiative. The features of these projects (e.g. increased open space, better air circulation, lower operational cost, better environmental quality, etc.) will be the “new normal” for most locators. The recovery of the office market will be driven by these new trends as the market continues to recover and with businesses returning to the office workplace.

Manila Office
10th Floor, Ayala Tower One & Exchange Plaza
Ayala Avenue, Makati City, 1226
t: (632) 752-2580
f: (632) 752-2571
w: www.santosknightfrank.com

Cebu Office
6/F 2Quad Building
Cardinal Rosales Avenue
Cebu Business Park
Cebu City, Philippines, 6000
t: (632) 260 0202

MANAGEMENT

Rick Santos
Chairman and CEO
Rick.Santos@santos.knightfrank.ph

OCCUPIER SERVICES & COMMERCIAL AGENCY

Morgan McGilvray
Senior Director
+63 917 865 3254
Morgan.McGilvray@santos.knightfrank.ph

RESIDENTIAL SERVICES

Marievie Gimena-Villanueva
Associate Director
+63 917 888 9087
Marie.Gimena@santos.knightfrank.ph

PROJECT MANAGEMENT

Andrew Frondozo
Director
+63 917 574 3055
Andrew.Frondozo@santos.knightfrank.ph

INVESTMENTS & CAPITAL MARKETS

Kash Salvador
Director
+63 917 865 5739
kash.salvador@santos.knightfrank.ph

FACILITIES & PROPERTY MANAGEMENT

Dennis Nolasco
Executive Director
+63 917 553 5646
Dennis.Nolasco@santos.knightfrank.ph

TECHNICAL SERVICES & ENGINEERING

Juvel Cedo
Business Development Manager
+63 917 635 8102
Juvel.Cedo@santos.knightfrank.ph

VALUATIONS & APPRAISAL

Mabel Luna
Director
+63 917 865 3712
Mabel.Luna@santos.knightfrank.ph

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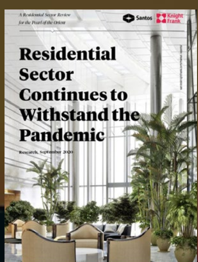

RESEARCH & CONSULTANCY

Jan Custodio
Senior Director
+63 917 574 3572
Jan.Custodio@santos.knightfrank.ph

Andy Enerio
Senior Project Analyst
Andy.Enerio@santos.knightfrank.ph

Angelo Manansala
Senior Research Analyst
Angelo.Manansala@santos.knightfrank.ph

Mirasol Bugas
Research Assistant - Santos Knight Frank Cebu
Mirasol.Bugas@santos.knightfrank.ph

Andrea Villadoz
Research Analyst
Andrea.Villadoz@santos.knightfrank.ph

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