Green Shoots

Philippine Real Estate Outlook 2022

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OVERVIEW

The Philippine property sector is poised to see a positive year of real estate activity in 2022 in the backdrop of an optimistic economic outlook for the country and the lifting of travel restrictions.

Santos Knight Frank expects a number of key themes in the office sector in 2022. Firstly, there is greater appetite for growth in the outsourcing sector in the Philippines due to demand from markets such as U.S., Australia, and Europe.

Secondly, tenants are likely to resume their delayed corporate real estate movements this year as low COVID-19 infection rates and lifted travel restrictions offer greater certainty for companies, with a number of companies already implementing return-to-office (RTO) programs. These decisions will include expansion, right-sizing, and adopting work and office setups (e.g. hybrid, hub and spoke, etc.) with a longer term foresight. Government policy, including PEZA incentives, will continue to affect real estate decisions.

Lastly, ESG will increasingly become a key concern among tenants albeit at a gradual pace. From Net Zero buildings to renewable energy assets, ESG is gathering pace as investors, landlords, and occupiers incorporate ESG considerations in real estate decision-making. One particular issue for companies will be the role of physical workplace in employee wellness.

While resilient sectors such as industrial & logistics will continue to thrive this year, one particular industry to watch are data centers. Santos Knight Frank forecasts that the country's emerging data center sector will likely double its supply capacity in the medium term, offering a number of opportunities to investors and landlords which are on the look out for new growth areas.

Meanwhile, the demand for residential properties especially in the condominium rental market in Metro Manila CBDs will likely pick up in 2022 – a result of re-opening borders, higher vaccination rate, and RTO programs. This sector is expected to get a boost from OFW remittances, which already grew by 5.1% in 2021 despite the pandemic. The anticipated positive year for residential comes amid an already strong demand for low-density residential spaces among affluent home-seekers during the pandemic.

From a capital markets perspective, investment-related public policies such as the amendments to the Foreign Investment Act, Public Service Act, and Retail Trade Liberalization Act are anticipated to encourage cross border capital flows to the Philippines. Furthermore, the listing of the sixth REIT in the Philippines – also the first non-office of its kind – is evidence that non-traditional income-generating assets such as energy are ripe to capitalize on the opportunities offered by REITs. The next question for REITs would be one of sustaining and increasing value. Strategies such as asset acquisition and retaining excellent property managers for both lease management and upkeep have been used by REITs in other markets, and we see these being adopted by Philippine REITs soon.

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THE OCCUPIERS' DILEMMA

Morgan McGilvray
Senior Director, Occupier Services
Morgan.McGilvray@santos.knightfrank.ph
Connect on LinkedIn

Agents or Benefits?

That's the difficult choice some BPOs are getting ready to make. Nicknamed as the Occupiers' Dilemma, BPOs might soon have to decide between keeping their PEZA benefits, or keeping a majority of their agents.

As of April 1st, PEZA-registered BPOs must bring 90% of their workforce back to the office. For the firms that don't bring back 90%, they risk losing some valuable PEZA benefits, such as income tax holidays and VAT exemptions. Many BPOs are reliant on these benefits, meaning that they'll look to comply.

But bringing back 90% of a workforce won't be easy. Most BPO agents have spent the last 2 years working from home, and the idea of being back in the office full-time may not be appealing. So BPOs must gauge their agents' willingness to report to office, and perhaps incentivize it, in order to avoid having issues with attrition in the coming months.

A solution to the Occupiers' Dilemma might be a compromise, such as the 70%/30% hybrid model that PEZA will propose to the next presidential administration. 70/30 would probably be enough flexibility for the BPOs to manage attrition, while still achieving the government's goal of stimulating the economies connected to PEZA zones. The industry is now hoping that the next government will agree.

Until then, demand for office space in 2022 should still be good, although market growth may not reach its full potential. Outsourcing firms will hedge some risk, by not putting too many seats in the Philippines until there's more clarity about benefits and attrition rates. That, combined with some expected office downsizing from the non-PEZA sector, will offset some of the BPO growth this year. But 2022 will still almost certainly be better than either 2020 or 2021, and growth could really take-off if a compromise such as 70/30 gets approval from the next administration. The BPO industry will have its fingers crossed until then.

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to explore the full article

THEMES IN THE OFFICE SECTOR

The Office as an Experience

New Workplace Models

Geographic Diversification

Flight to Quality

WORKPLACE CONTINUES TO EVOLVE

The office will look more like a playground: A place of experience

Amenities APAC occupiers expect staff to demand in the next three years.

F&B offering
54%

Healthcare facilities
46%

Gym facilities
39%

Drop & collect parcel facilities
54%

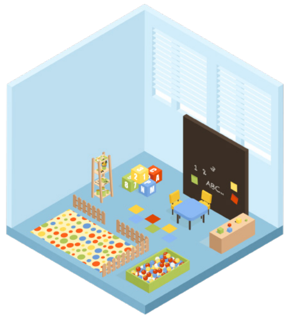
Free food and drink
36%

Facilities that support mental well-being (e.g. sanctuary spaces)
33%

Cycle storage & facilities
33%

Concierge
31%

Childcare facilities
27%



Educational Programs & facilities
17%

Survey from Knight Frank's (Y)OUR SPACE - 2021 report, which covers occupier trends & the changing workplace. It draws on responses from almost 400 international businesses with a combined headcount in excess of 10 million, providing unique insight into the workplace strategies and real estate needs of global companies. The survey was conducted between December 2020 and February 2021.

PEOPLE, ENVIRONMENT & TECHNOLOGY: THE TRIUMVIRATE OF PROPERTY & FACILITIES MANAGEMENT IN 2022

Dennis Nolasco
Head of Facilities & Property Management
Dennis.Nolasco@santos.knightfrank.ph
Connect on LinkedIn

Embracing new technologies

When the workplace goes digital, there must also be proper digital governance. There are many organizations digitizing their processes and operations, such as shifting to cloud-hosted technologies in helping them make important decisions.

This gives many benefits for facilities and properties to make use of the efficiency and convenience that technology can provide such as real-time data which cannot be done in a non-paperless setting. This shift highlights the increasing importance of data and making use of technology such as Artificial Intelligence (AI), Internet of Things (IoT), and machine learning which can help break down and manage information for faster analysis, interpretation, and execution.

Prioritizing wellness, health and safety

The pandemic has led to habits that promote good hygiene standards which will likely continue to exist long after the pandemic. Such practices include the installation of hand sanitizers throughout common areas, the improvement of ventilation in the office, and routine sanitation checks in areas with high touchpoints. Measures like social distancing, a one-way system, and face mask zones are also part of these safety practices. Facility managers will be expected to continue upholding these practices and ensuring that all measures will be in place moving forward.

But there is also a deeper conversation about health and that is on the mental wellbeing aspect of employees. A staggering 53% of 6,000 respondents in a study conducted by mental health firm MindNation in 2021 reported worries on financial and health pressures. Around 35% said productivity had been affected, and more than 1 in 10 considered taking more sick leaves due to mental challenges. Companies will need to continue prioritizing and addressing wellbeing even as the pandemic becomes better managed and the economy re-opens, and this has important implications on the ways workplaces will be designed and operated.

Emphasis on green

Sustainability is not a new agenda for companies, but the pandemic has accelerated the green conversation, with now a firmer resolve to see things through. Now more than ever, there is greater interest on Environmental, Social, & Governance (ESG) in both the occupier and the landlord/investor side. This is driven not just by the competitive advantages and financial benefits it provides, but also the realization that 40% of carbon emissions around the world are attributed to the real estate sector. Topping the ESG agenda is energy efficiency, which Asia Pacific investors surveyed by the Urban Land Institute identified as the No. 1 ESG consideration in 2022. Designing or redeveloping buildings with sustainability in mind is something that companies can do to support their carbon targets.

DATA CENTERS: THE PHILIPPINES ON THE RADAR FOR INVESTMENTS

Monica Gonzalez
Director, Occupier Services | Data Centers Lead
Monica.Gonzalez@santos.knightfrank.ph
Connect on LinkedIn

The data center market in the Philippines has seen more movement over the last six months than the last two years, making it one of the fastest-growing real estate sector in the Philippines.

The reasons are not difficult to perceive. We create 1.7 MB (or roughly the size of a photo taken from your mobile phone) every second. All of that data is stored in a data center somewhere in the world.

COVID-19 has only accelerated our reliance on data centers. With more video calls and hybrid work happening around the world, we are seeing greater dependence on technology. The demand for colocation, internet, and cloud services requires the need for sophisticated facilities based in-country.

It is no surprise therefore that the global data center market is estimated to grow at an average of more than 13% ever year to USD 143.4 billion by 2027, according to Research and Markets. By 2023, Asia Pacific is predicted to account for 30% of global center revenues. Excitingly, the Philippines is near the epicenter of this wave of developments happening across the region.

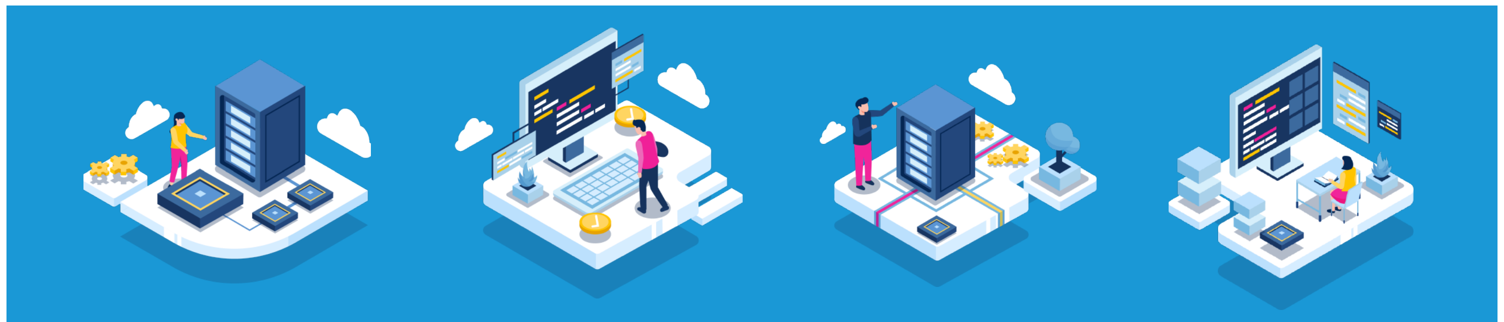
The country has been on the radar for data center operators as an emerging market with great potential in the Southeast Asia region, primarily for the local population's high digital consumption. The number of internet and social media users in the Philippines rose by 6.1% and 22% respectively between 2020 and 2021, according to Hootsuite.

This is supported by a wide array of characteristics that make investing ideal in the country, such as government support, the growing renewable energy sector, and availability of engineering and IT talent. Infrastructure development has also been an appeal; the Philippines' infrastructure spending will average about 5.4% of GDP between 2022 and 2024, a considerable investment in accessibility. Lastly, the country offers an important factor that some established hubs cannot: available raw land.

What can we expect over the medium term? While the country currently has a total IT supply capacity of 94 MW, Santos Knight Frank has recorded approximately 125 MW of additional planned capacity from regional and international operators who expressed interest to build in the medium term.

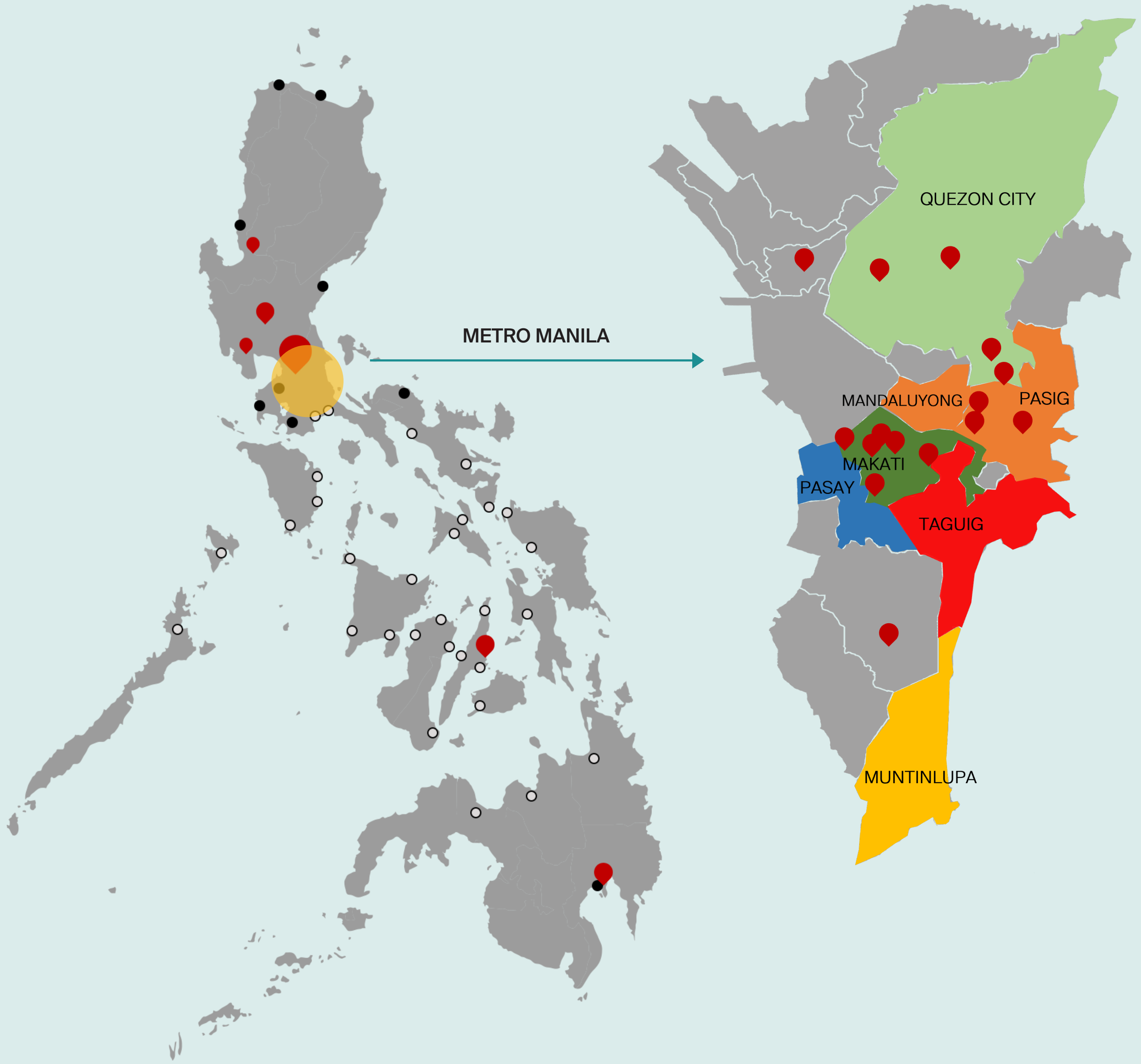
Already, first-mover YCO Cloud Centers has announced the construction of a world-class 12-MW data center in Malvar, Batangas. The Tier III/ Tier III+ compliant data center will feature a purpose-built 10,000-sqm, two-storey facility with four 3-MW data halls.

The data center market is an exciting space for the Philippines. As the data center sector continues to grow alongside the increasing demand for data, we expect to see an upswing in activity for data center investments into the country.



SUPPLY

Santos Knight Frank estimates that the Philippines' data center IT supply capacity will more than double in the medium term.



- Location of upcoming data centers
- Data center / cluster of data centers
- International subsea cable landing points
- Domestic cable landing points

Total capacity

94 MW

Expressed interest

125 MW

INDUSTRIAL SECTOR: RIPE FOR REAL ESTATE EXPANSION

Kash Salvador
Head of Capital Markets, Santos Knight Frank
Kash.Salvador@santos.knightfrank.ph
Connect on LinkedIn

Opportunities continue to shine bright for the industrial & logistics sector. Long-term structural fundamentals have positioned this sector as one of the most resilient asset classes during the pandemic.

One of the drivers of that growth is e-commerce. It is estimated that shopping app penetration among Internet users in the Philippines is nearly 86%, according to Statista. Meanwhile, Philippine e-commerce revenues are expected to increase from USD 4.42 billion in 2021 to USD 7.67 billion in 2025.

Across Asia Pacific, Manila has one of the lowest average prime warehouse rents – an advantage of the Philippines that keeps operating costs down and supports faster expansion. The average prime warehouse rent in Manila has remained relatively stable at PhP 235/sqm/month during the second half of 2021, according to Santos Knight Frank. With strong demand, lease rates are expected to increase over the next 12 months.

Supply of fully equipped storage facilities has become a challenge among occupiers. This, in turn, is a new area of opportunity for real estate players. With much of supply around Metro Manila concentrated in Calabarzon, it is anticipated that real estate players will focus industrial & logistics developments in underserved areas with good accessibility and infrastructure, such as North Luzon.

In the capital markets side, REITs have recently become an option for real estate players to generate capital. REITs have so far mostly concentrated on the office sector. With the performance of the industrial and logistics sector, it will likely be just a matter of time before the Philippines sees more alternative assets listed as REITs.

ASIA PACIFIC PRIME WAREHOUSE RENTS

Market	City	USD / sqm /month	6-month change	Forecast next 12 months
Australia	Brisbane	7.18	4.4%	↑
	Melbourne	6.36	5.0%	↑
	Sydney	9.81	5.9%	↑
East Asia	Tokyo	12.01	0.8%	→
	Beijing	9.69	0.5%	↑
	Shaghai	7.87	4.0%	↑
	Hong Kong SAR	27.64	2.2%	↑
	Taipei	12.96	3.1%	↑
India	Bengaluru	2.72	-4.6%	→
	Mumbai	6.93	-7.8%	→
	NCR	2.59	1.1%	→
ASEAN	Jakarta	4.88	2.8%	→
	Kuala Lumpur	4.91	0.0%	→
	Singapore	13.89	-4.9%	↑
	Bangkok	4.76	0.5%	→
	Manila	4.60	0.0%	↑

Source: Knight Frank Research

HOW SECOND HOMES HAVE BECOME FIRST PRIORITY

Marievie Gimena
Associate Director, Residential Services
Marievie.Gimena@santos.knightfrank.ph
Connect on LinkedIn

The need for great quality homes has never wavered during the pandemic. While one cannot help but see the easing of pandemic-induced restrictions and rising economic activities as a boost for the residential sector (especially condominium rental), the overall resilience of the residential sector comes from the fact that houses are a necessity and fill the basic need for safety, security, and comfort.

During the last two years, people have spent more time within their homes than they have ever since their childhood. This has spurred the requirements for spacious, open, and green homes to address needs such as work-from-home setups, greater dependence on energy and technology, prevention of cabin fever, and wellness.

Choosing a home, whether a condominium or a house and lot, still comes down to good location. A place or hometown with proper access to essential establishments such as convenience stores, markets, and institutions such as schools, hospitals, government centers, and the like is probably one of the best homeowners' realizations. But the adage of location, location, location has taken a new meaning after the pandemic experience. While people want to be within reach of convenience, there now also seems to be greater desire for locating near places of leisure, nature, beach, and mountains.

When we asked high-income Filipino buyers whether the pandemic has encouraged them to buy a second home, 41% said yes – one of the highest in Asia Pacific*. We have seen "workations" becoming a trend where people stay in places for a different scenery or breath of fresh air away from a locked down city. Interestingly, the team has seen an increased demand in leisure destinations mostly from higher-income buyers.

The need for second homes is likely to stay, caused by a myriad of factors. The improvements in infrastructure are one, cutting down on travel time between Metro Manila and destinations such as Batangas, Baguio, La Union, Subic, and places of interest. WFH is another, having made the last two years a great big experiment and proving that WFH can work for certain sectors. Lastly, health and wellness have become a priority.

Shifting and returning preferences

Meanwhile, we anticipate movements in other sectors of the market, too. The condominium rental market in Metro Manila has started to pick up since last quarter of 2021 and a robust demand this 1st quarter of 2022.

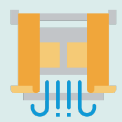
In the primary sale market of condominiums in Metro Manila, average prices have increased slightly by 1% to PHP202,000/sqm in Q4 2021 versus the previous quarter. There is also a greater appetite for bigger cut units (such as 2BR and 3BR), driven by families upgrading their homes and high-income parents and breadwinners providing real estate as inheritance ("pamana"); and OFWs. Overseas remittances, which have been sources of funds to acquire residential properties and drive consumption, grew by 5.1% in 2021 versus the previous year.

The recovery across the economy in 2022 will likely impact home prices, which have stalled during the pandemic. As prices bounce back this year, buying one's primary or second home is increasingly becoming a "now or never" kind of situation.

*Global Buyer Survey: The Philippine Edition 2021

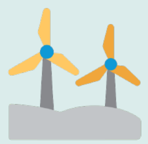
PENT UP DEMAND
49% said budgets for home acquisition have not changed despite the pandemic

LOCATION PREFERENCES
40% prefer the suburbs, while 33% the city for their next homes

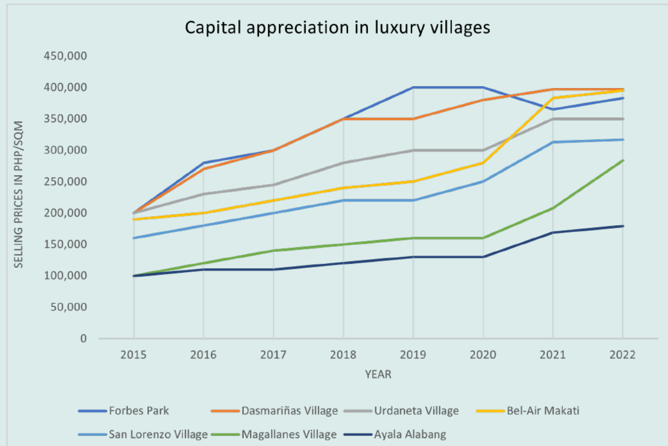


FRESH AIR
Preference for low-density spaces and house & lot

SECOND HOMES
41% want to buy second homes, higher than Asia's average (27%)



ENERGY EFFICIENCY
40% prefer the suburbs, while 33% the city for their next homes



Source: Santos Knight Frank Research

THE INDUSTRY MUST LEAD ON NET ZERO

David Goatman
Knight Frank's Head of Energy, Sustainability and Natural Resources
David.Goatman@knightfrank.com
Connect on LinkedIn

COP26 in Glasgow was an opportunity for the real estate industry to showcase its commitments, and to engage in dialogue with governments from around the world on the opportunities, as well as the challenges, that net zero brings.

But as attention turns to this year's COP27 event in Cairo, what is the legacy of COP26, and what progress is needed before it?

November 2021 saw the first formal Built Environment Day at COP since Paris in 2015. The conference was teeming with representatives from the property sector focused upon addressing the sector's significant contribution to global emissions, approximately 40% globally.

Among the commitments brought forward, the World Green Building Council announced 44 new signatories to its Net Zero Carbon Buildings Commitment, which aims to halve emissions in the built environment sector by 2030 and achieve net zero carbon emissions by 2050 at the latest. The businesses and organisations that signed up represent an annual turnover of more than $100bn, reflecting the weight of support behind the industry's net zero goals.

However, the text produced through intergovernmental negotiations at COP26 does not once mention the role of business in the global effort to slash emissions and combat climate change. Despite this glaring omission, attendees left with the conviction that net zero is fundamental to future business strategies. Net zero objectives bleed into every level of the corporate value chain. For real estate, we are clearly seeing the effects.

As Knight Frank's Active Capital 2021 report found, prime central London offices with a BREEAM New Construction 'Excellent' rating enjoy a 10.5% premium on sales price compared with equivalent unrated buildings. This is mirrored globally. Prime office buildings in Melbourne and Sydney with a NABERS rating of 5+ enjoy a 17.9% premium on sales price compared with equivalent unrated buildings.

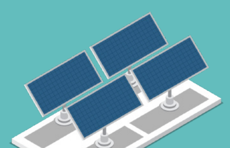
The question, in light of the COP26 text's omission of the role of business, is how the industry can work with government to further collective net zero goals

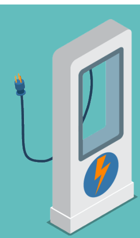
Government naturally seeks policy levers by which it can drive change quickly and visibly. A key lever for decarbonisation in commercial real estate has been the Minimum Energy Efficiency Standard. This legislation had a marked impact on behaviour and attitudes, with targets now accelerated to a minimum 'C' by 2027 and 'B' by 2030.

The challenge is finding more 'levers' by which government can work with the private sector to meet net zero targets. While the sector is exploring new opportunities with natural climate solutions, for example, these often straddle multiple government departments, making them difficult to progress at policy level.

In our markets, we see increased focus upon the investment opportunity presented by natural capital projects, particularly land use focused upon carbon sequestration. This is an obvious example of where forward-thinking policy could unleash substantial capital and accelerate a wide range of new projects.

With the official COP text silent on the role of business, it will be for the global industry to take the lead on progressing toward net zero's goals. The market is demonstrating how sustainable buildings and places create value, and in many ways private sector innovation is overtaking policy, with governments around the world playing catch-up.





NEXT STEPS IN 2022

As property owners, landlords, and investors seek out growth, diversification, and recovery this year, they face the following opportunities

1. A time for acquisition

During the pandemic, the market has seen an increase in the number of properties for sale across several sectors of real estate. Buyers can leverage on the wider range of options and flexibility in pricing to make the best real estate investment decisions.

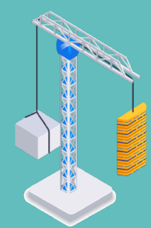
2. Watch out for gentrification

More old neighborhoods in Metro Manila will likely experience gentrification as the economy picks up steam in the road to recovery. A number of factors are driving this growth: The work-from-home setup that spurred consumer demand within urban residential areas, the improvement in urban infrastructure, and appetite for growth by developers, among others.

3. Growth areas with infrastructure are prime for development

Areas along new thoroughfares in North Luzon and Southern Tagalog such as the Cavite Laguna Expressway (CALAX) and the Tarlac Pangasinan La Union Expressway (TPLEX) offer opportunities for industrial, commercial, and residential developments. These are, most immediately, the ones best primed for activities.

SECTORS IN THE SPOTLIGHT

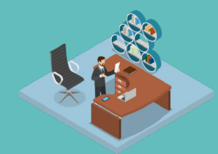


INDUSTRIAL

Demand for industrial properties will continue to be strong. With low supply of fully equipped facilities and properties that can cater to size requirements, developers have an opportunity to capitalize on this sector in 2022.

DATA CENTERS

Supply of IT capacity is estimated to double in the medium term.



OFFICE

The office remains to be a stable and long-term investment especially as the Philippines recovers from the pandemic.

RESIDENTIAL DEVELOPMENTS

Gentrification of old neighborhoods and the rise of suburbs make residential developments, such as townhouses and single-detached homes, an ideal investment.

LEISURE

The pandemic has not dramatically changed people's desire for leisure and relaxation. As travel restrictions are lifted, pent-up demand for tourism will be advantageous to the leisure sector.

HEALTHCARE

The pandemic has emphasized the value of health, wellness, and safety. Healthcare real estate is ripe for further expansion.

Santos Knight Frank is the first and largest fully integrated real estate services company in the Philippines. Founded by Rick Santos in 1994, he has grown the business to 11 market-leading service lines and over 1,400 professionals across the country. Santos Knight Frank is responsible for more than 4 million sqm of office space transactions, including the largest office leasing deal in Philippine real estate history, and today manages 20 million sqm of property. Santos Knight Frank was named “Best International Leasing Agency” during the International Property Awards 2021.

The company is part of the **Knight Frank** global network. Founded in 1896, Knight Frank LLP is the leading independent global property consultancy. Headquartered in London, Knight Frank has more than 16,000 people operating from 384 offices across 51 territories. The Group advises clients ranging from individual owners and buyers to major developers, investors and corporate tenants.

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For a private consultation about the report or your property, contact us.

Email: pr@santos.knightfrank.ph
Call: +632 7752 2580 or +63 917 874 3532

Editorial Team
Paolo Abellanosa
Ria Lontoc

Design & Layout
Alec Valerio

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